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Supply Chain Lessons from 2019

A guide to navigate global trade challenges in 2020 and beyond

Introduction

Uncertainty. Unpredictability. And, added complexity. From the tariff whiplash that played out during 2019 and continues to unfold, to the start-stop-stall of Brexit, to confusion surrounding the readiness and anticipated impact stemming from IMO 2020 regulation, **businesses have been hit hard**.

Add to that the prospect of a potential global recession on the horizon, and—at least outside of the US—a renewed commitment to affecting climate change worldwide. Global trade is facing unprecedented challenges and opportunities. The traditional modus operandi of shipping goods no longer applies. Read on for insights on how to better lead your organization forward in the year ahead.

1 The Modern Era Has Ushered in a Set of C-Changes

Businesses have had to rethink their business models and supply chains, tapping new strategies. Their objective: to stem the tide of lost revenue due to trade war tariffs and more stringent regulations. But also to find new paths to consumers in the face of the 'retail apocalypse' that has continued to take out well known and established retail stores. And that's especially important since it's not just the retailers that are impacted—it's also the brands that are relying on those stores for distribution.

Four key themes have converged to spur the need for setting a new foundational approach to global trade.

1. Complexity

An already complex industry has become more so due to new tariffs and customs regulations. There has never been a greater need for transparency, actionable data analytics, and expertise to navigate trade disciplines to preserve margins and overall business health. The sometimes weekly changes in tariffs, have necessitated more nuanced understanding of duties and customs laws in order to protect the bottom line and ensure goods get where they need to go on schedule.

2. Cost

The US-China trade war has hurt businesses that have absorbed tariff hikes in an effort to shield consumers from markups on pricing to offset the duties levied on their goods. "We've seen a steady stream of tariff increases. Uncertainty in 2018 led to a decline in the GDP of 0.8%, which showed up in the first half of 2019. You have uncertainty about uncertainty," observes Dr. Phil Levy, Chief Economist for

Flexport. The result: A ripple effect has taken place. To mitigate added costs, companies have scaled back or relocated manufacturing, as well as reconfigured parts of their supply chain.

3. Competition

The world of e-commerce has completely altered customers' expectations around service and delivery. Retail outlets that have stuck with the status quo have fallen. And, brands that rely solely on those brick-and-mortar stores for distribution have also been hurt. As a result, upstarts are grabbing market share from businesses that have been around for years. As we've seen with brands that have survived the 'retail apocalypse,' organizations must provide more ways for their customers to experience their brand. More noteworthy, consumers want faster delivery and have much lower tolerance for stock-outs. Competition has intensified.

So in that reality, what have we learned?

- The old way of doing business — with one fulfillment center — has gone the way of the dinosaur. To meet the expectations of two-hour delivery windows, brands need far more fulfillment centers.

- To be competitive, organizations need to accelerate the business cycle from end to end as fast as possible, from the factory on into customers' hands.

All of this spurs the need to find new ways to delight customers. The name of the game: varying levels of brand engagement. The unfortunate reality is that those that don't, and stick with the status quo, find themselves being sucked into the 'retail apocalypse.'

[1] Target shares hit record highs after the retailer blows out earnings estimates, CNBC

Interestingly, some companies that were originally on the death-knell list are doing massive turnarounds, recognizing that traditional ways put them in danger. Target is a great example. In 2018, the store was on Business Insider's list of retailers that were closing shops. Fast forward to August 21, 2019 when they blasted Wall Street's earnings expectations and automatically became a retail hero. As CNBC reported at the time, Target shares surged 20%, closing at a record $103 a share. The lift raised Target's market value to $52.7 billion, up from $43.819 billion on August 20.[1] "Target took advantage of transforming the physical and the digital to make themselves relevant to customers, offering multiple forms of brand engagement in store and online," says James Chen, Flexport Chief Technology Officer. "Doing that right means changing the distribution model from one to many, which requires technology that enables seamless collaboration and transparency."

4. Climate

Rising concern about climate change and sustainability, along with regulations like IMO 2020, are having a profound impact. At United Nations Climate Summit Action 2019, 65 countries vowed to cut greenhouse gas emissions to net zero by 2050, and 70 countries announced a renewed commitment to take action to improve environmental stewardship. At the same time, in the business sector, more than 100 leaders announced firm action plans to meet Paris Agreement targets and accelerate the move from a grey to green economy.[2] Organizations will increasingly be held to a higher standard—if not by law, then by concerned citizens, many of whom are likely to be customers or investors.

[2] Climate Action Summit 2019, UN.org

And if peer pressure from businesses and nations isn't enough, there's regulation to stir the pot. At Flexport's September 2019 customer event, FORWARD, Jamie Webster, Senior Director, Center for Energy Impact from the Boston Consulting Group (BCG), referred to the International Maritime Organization's (IMO) introduction of new fuel requirements as "the biggest planned disruption in the history of energy markets."[3] That's because while IMO 2020 will hit oil refiners and carriers first, others involved in global trade can expect to see knock-on impact. The regulation, which goes into effect on January 1, 2020, mandates the sulfur content of marine fuel oil to be reduced from 3.5% to 0.5%. In addition, the IMO intends to cut total annual greenhouse gas emissions by 50% by 2050, compared to 2008, while working toward phasing them out entirely."[4]

[3] IMO 2020 Regulation: Are You Ready, Flexport

[4] Low carbon shipping and air pollution control, IMO

To successfully move forward in today's era of unpredictability, business leaders must ensure their logistics and supply chain managers are equipped not just with the right tools, but the right data services, industry expertise, and strategically aligned transportation and warehousing infrastructure.

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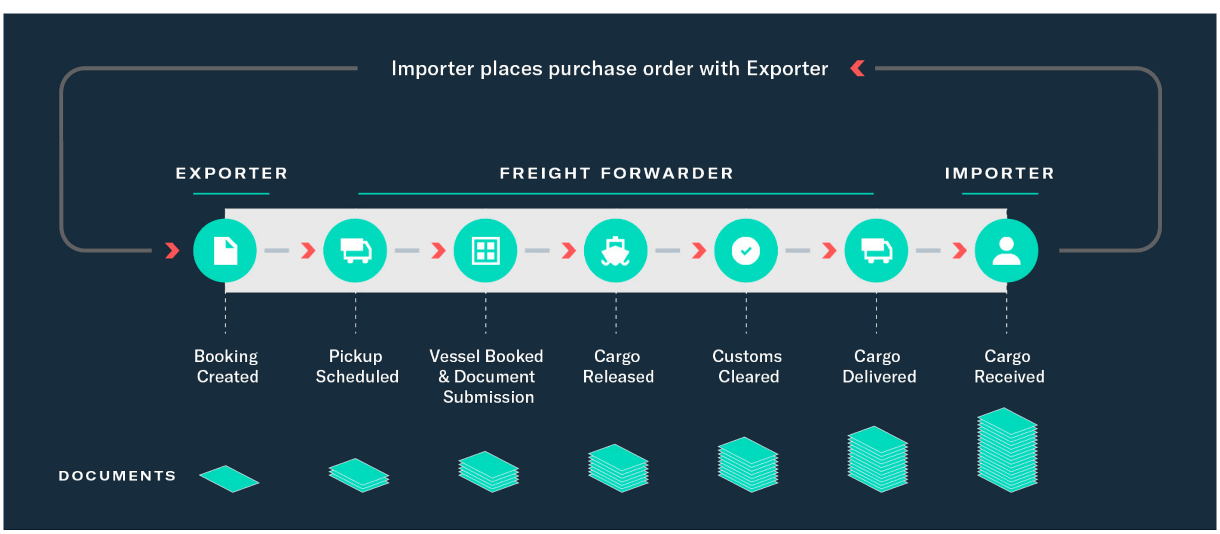
C-Changes Require T-Changes

1. Technology

In the world of higher competitive stakes and uncertainty across the global trade landscape, the winners are those who know how to simplify the complex with more visibility, more predictability, and greater efficiency to create customized experiences. And, data will be central to making that happen. In 2020, we can expect digital transformation to become even more critical in the race to keep up with changing customer expectations, governmental regulations, and tighter competition.

As the illustration shows below, there are typically eight phases involved in moving goods from Point A to Point B, all of which can be taking place in different parts of the world. With each phase, the documentation required grows in volume and complexity—leaving ample room for error and delays, which can have a ripple effect throughout the supply chain. Through it all, multiple stakeholders, such as freight forwarders, factories, suppliers, manufacturers, truckers, regulators, and more are navigating their individual industry regulations to ensure business success from one part of the world to another.



That kind of complexity is ripe for tools to simplify the process and drive significant efficiency and productivity along the way.

In Flexport's technology platform, for instance, a dashboard with customizable features like filter views, real-time shipment-tracking maps, and other functionality lets teams zero in on what matters most, so they can prioritize their work during fast-moving processes.

- In fact, Beta customers testing the latest upgraded version of the dashboard were finding the information they needed 30 to 40% faster.

In addition, the platform helps teams align specific shipments with business priorities through specialized references. Shipments can be grouped and tagged with references that are consistent across all parties all the way through the shipping process.

- The benefits: better planning, more insightful reports and analytics, and the ability to identify areas for improvement across the supply chain.

A third major innovation improves collaboration between shippers and their suppliers. Tasks can be assigned to partners in the supply chain, questions or concerns can be flagged—delivering sorely needed transparency. Moreover, the technology enables automation and reuse of data. So as the volume of documentation grows during the shipping process, the time involved filling out forms becomes less burdensome. Being able to pre-populate docs with data entered previously, helps provide greater time savings.

- Shippers can complete tasks within minutes and reduce the possibility of errors. Beta customers testing newly rolled out features found they could complete bookings up to 60% faster with 4 to 4.5x more accuracy, saving them from having to chase emails.

For a more effective supply chain and quicker decision making, look for technology that offers the following advantages:

- Real-time shipment tracking at each step of its journey, with intelligence to highlight exceptions and delays to ensure you have the product inventory needed to meet customer demands
- Powerful analytics that can show trends in volume, spend (including landed cost per unit), and delivery time, with details down to the SKU level
- Customizable reports that can be exported to many file formats with a single click
- Transparent communications to message colleagues, suppliers, and your freight forwarder in context, to spend less time sifting through email
- Easy-to-reconcile quotes, invoices, and billing functionality with detailed reporting that holds every party accountable

2. Tariff & Trade Advisory Services

Trying to plot business strategy in the midst of a trade war can be a bit like playing a chess game. Putting that in perspective, Tom Gould, Vice President of Customs and Trade Advisory, notes, “Between 2018 and 2019 we saw more changes in the tariff than in the past 10 years combined.” On top of that, there was a 49% increase in penalties issued by United States Customs and Border Protection (CBP) between 2017 and 2018, jumping from 931 to 1,385.[5] Many believe this is just the start of more to come.

[5] Trade Statistics, US Customs and Border Protection

But there's good news. Data, expertise, and technology can help inform strategies to mitigate tariff impact. For instance, referring back to the 18-month period of record-setting tariff changes and increased penalties, Gould pointed out that customs inspections for Flexport shipments dropped substantially, due to the data integrity of Flexport's technology.

And while technology and data are valuable partners in the process, so are humans who understand the nuanced complexity of trade and tariff regulations.

As an example, customs experts can provide strategic insight around 'substantial transformation'—a customs principle that determines the country of origin of a product, for the purposes of assessing duties when an item that's being traded doesn't come wholly from one country. So, let's take a pair of jeans. What if the fabric is made in China and cut to the basic pattern in China—but the pieces are sent to Vietnam for sewing, embellishment and finishing?

Deep understanding of customs and tariffs can help determine how to classify products to avoid paying higher customs duties. For instance, sometimes products can overlap categories that impose dramatically different costs. Case in point: Tariffs on backpacks are higher than hydration packs. By piercing the surface of regulations, trade advisors can explore possibilities to identify legitimate solutions to mitigate tariffs and customs duties.

Knowing how to steer through the complexity of the constantly evolving regulations, can enhance any company's ability to be more agile—and avoid stalls in the shipping process.

3. Transportation Strategies and Services

For those not involved in the day to day of shipping, the intricacies of transport logistics and decision making can be hidden. As mentioned earlier in this paper, IMO 2020 will have a huge impact on the ocean freight market. According to research from BCG, "Compliance will result in an additional $25 billion to $30 billion in fuel costs for container liners from 2020 through 2023. The annual increase will be highest in 2020, reaching an estimated $10 billion to $12 billion...."[6]

[6] IMO 2020 Regulation: Are You Ready, Flexport

The imposed move to lower-sulfur fuel will also have implications on air and rail. Businesses can expect to see pass-through costs in 2020, which, in some cases, have already begun.

To navigate industry challenges more easily, look for experts who understand market fluctuations in cost and capacity. By seeking out professionals who are familiar with transport strategies that map to business objectives, you'll be better positioned to rein in costs, mitigate tariff impact, meet carbon emission goals, and operate with agility.

When it comes to shipping, knowing your company's needs regarding cost and time is everything.

In the world of ocean freight, businesses pay for speed or space. LCL—or less-than container load—lets you ship in smaller volumes to keep inventory lean. With goods from multiple businesses on the same shipment, however, it requires additional steps and time.

FCL—full container load—on the other hand, is faster. However, if you haven't maximized the capacity, you might be paying for wasted space.

For businesses that don't have the volume to justify FCL, the waiting game can be painful—especially during peak season, times of crunched capacity, or looming tariff deadlines.

When neither LCL or FCL are viable alternatives, a hybrid solution makes sense. After data in 2018 showed that most containers ship one-third empty from China to the US, Flexport rolled out a solution called OceanMatch. Designed to reduce expense and environmental impact, Flexport uses structured data to identify empty space that has already been booked and paid for—then, it buys that space back and sells it to other businesses trying to get goods shipped. This has helped cut shipping costs for Flexport customers by an average of 19% per sailing compared with FCL. Plus, 100% of carbon emissions are offset. Good for the bottom line, good for the environment.

While most organizations naturally choose to ship by ocean to avoid the expense of air, there are times when air is warranted, such as during holiday rush or other time-sensitive events. Having access to private air services that have more flexible scheduling can ensure goods get where they need to go, while beating tariff deadlines. As an example, when the September 1 tariffs were about to hit in 2019, Flexport leveraged airfreight to land customers' goods 15 minutes before the midnight deadline.

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Beyond the Fundamentals: Additional Considerations

With the possibility of more tariffs to come, along with more uncertainty and more tumult in the market, two additional elements merit consideration: freight financing and freight insurance.

1. Freight Financing Fuels Growth

Between tariff hikes and trade wars, emerging geopolitical factions and a looming potential for recession, executives and logistics managers need new ways to stay agile in the face of trade turbulence. One way to do that: freight financing. By taking a closer look at production and logistics strategies and supply chains, financial executives can reallocate working capital to drive growth.

During 2019, Flexport financed roughly $140 million of working capital, helping clients to:

- Negotiate larger orders at lower prices
- Expand manufacturing facilities
- Stabilize variable overhead
- Ship goods before peak-season rates
- Build inventory to switch to lower-cost transportation options
- Invest in marketing
- Start new business units

2. Insurance is Not Just a Nice to Have

In addition to tariff whiplash, the past year also saw port strikes, political unrest, and lack of a true peak season. These factors have posed obstacles to planning and forecasting—and have created conditions inherent with risk. Based on information provided by Roose & Partners Casualty Newsletter, in Q1 2019, there was an average of two cargo ship accidents per day.[7] Flexport data on claims for its insurance program from 2018-2019 shows most damage occurs en route, to and from port. Long story short: Shipping is risky, and without the appropriate insurance coverage, costly.

[7] Casualty Newsletter, editions 301-313, Roose & Partners

The right policy can help offset hits to revenue due to marred goods. And, in the case of lost or damaged ocean shipments, it can help defray additional costs to expedite shipments via airfreight to replace those goods.

Keep in mind:

- Carriers are not financially liable for the full value of merchandise. In the event of any damage or loss to a shipment, the carrier will likely have limited liability under international conventions.
- Most carriers and insurance policies don't provide coverage when freight is held at port. Shippers should check if their policies provide coverage for detention and demurrage or help during disruptions that cause delay.
- Ocean carriers typically limit their liability and settling claims can take months. Businesses should seek insurance that offers value and flexibility. Flexport, for instance, offers insurance with a $0 deductible and settles claims for $10,000 or less within five to 15 days.

3. Social and Environmental Impact

IMO 2020 is not just a challenge, it's an important step toward reducing pollution. Case in point: If the shipping industry were a country, it would be the world's sixth largest polluter. For individual companies, shipping can account for more than 50% of their total carbon footprint. But it's an often overlooked opportunity to make a huge impact. According to Stanford University's Center on Philanthropy and Civil Society, more than 90% of CEOs state that sustainability is important to their company's success.[8]

[8] The Next Phase of Business Sustainability, Stanford Social Innovation Review

So how can businesses take action?

Shipping carbon neutral is a great way to reduce impact on the environment. Flexport makes this easy with its carbon offset program.

Also, brands that show concern for the environment and the communities they operate in stand out and can benefit in the process. For instance, when companies import goods that are not sold, and instead donate them internationally, they can file with US Customs to get their duties back.

In addition, most cargo insurance policies require that damaged goods be destroyed or thrown away. However, Flexport insurance lets companies donate merchandise that is still usable. Flexport.org, Flexport's program supporting nonprofits and NGOs, can match damaged goods with those in need.

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Conclusion

To make sure your business is primed for all that 2020 has to offer, consider these five questions:

1. How is your freight forwarder helping to solve the intricacies of tariffs and customs?

2. How does technology help your business keep up with current challenges in global trade?

3. What supply chain management tools are you using to position your company for fast fulfillment?

4. What are you doing to meet or beat corporate goals while reducing impact on the planet?

5. Do you have access to actionable data insights from your freight forwarding to plan strategy and execution?

6. How are you mitigating risk to shipments?

Remember, what might appear to be less expensive upfront could be more costly over the long haul. Look at the big picture, as well as the main focal areas:

- Check landed costs of goods.

- Explore how to bring greater transparency, ease of decision making, and agility to your business shipping.

- Understand the opportunities and limitations of customs laws.

- Make sure your freight (and bottom line) is protected with insurance.
- Consider how you can improve agility with better inventory distribution through freight financing.

Taking the right steps to address the challenges and opportunities expected to unfold in 2020 better positions your company for success. By doing so, you're able to empower operations to focus on making great products and delighting customers; optimize the business for agile positioning to meet demand; and reduce carbon emissions to make the world a better place.

To learn more about how to ready your supply chain for what comes next, talk to a Flexport expert: https://flx.to/FutureProof.

Helpful Resources

Tariff Insider

Customs & Trade Advisory Services

Import Duty Calculator

Weekly Freight Market Update

USTR Info on Section 301 Tariffs

Flexport Carbon Offset Program

About Flexport

Through its Operating System for Global Trade, Flexport delivers a strategic model for global businesses that combines advanced technology and analytics, logistics infrastructure, and hands-on supply chain expertise. Delivered to customers and suppliers via a highly available and secure cloud software platform, Flexport's Operating System for Global Trade enables fast and reliable transit times, greater visibility and control, and low and predictable supply chain costs.

With its cloud software and data analytics platform, Flexport today serves almost 10,000 clients and suppliers across 109 countries. Its offerings span ocean, air, truck and rail freight, drayage and cartage, warehousing, customs advisory, financing, and insurance.

Learn more at flexport.com