White Paper

How to Activate Agility During Major Disruptions in Global Trade

Emerging from COVID-19: A Supply Chain Analysis with Boston Consulting Group

Introduction

Even as the world of global trade was trying to right itself from waves of disruption due to trade wars, uncertainty around the on and off status of Brexit, and the fallout of new environmental standards introduced by IMO 2020, the signs of a weakening global economy were beginning to loom large. Then came the COVID-19 pandemic, creating unprecedented levels of unpredictability and completely turning supply chain management inside out.

This white paper, a collaborative effort with Boston Consulting Group (BCG), offers suggestions to help inject agility and resiliency into your organization despite challenging market conditions. Read on to discover lessons learned from the pandemic: how to emerge from massive disruption in the midst of chaos no matter what the source, and transform operations and strategy during the interim between rebooting from the pandemic and facing a new, post-COVID-19 reality in the months to come.

And We Thought 2019 Was Tough

Global trade is no stranger to disruption, but the COVID-19 health crisis will go down as an exceptional event for businesses, the world economy, and especially supply chain management.

Two aspects of this crisis, in particular, have made it unprecedented for supply chains.

First, the geographic extent of the disruption has been vast and simultaneous. Even if supply chain players have dealt with temporary and geographically localized disruption due to climatic events, wars, strikes, and other situations, they have never had to deal with a disruption affecting the entire world and the full set of transportation and logistics all at the same time.

Second, the disruption of supply chains has been the transmission belt of this crisis, enabling the health pandemic to expand to become an economic disaster.

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Unexpectedly, within a very compressed timeframe, businesses have had to learn how to conduct operations from home, while stores were forced to reinvent themselves, pivoting from brick-and-mortar to e-commerce; from B2B to B2C; from in-store to curbside. It's no longer about fixing issues of moving goods from Point A to Point B. It is now far wider than that: a complex equation of supply and demand—and transport and storage capacity—as the already challenging endeavor of forecasting has become wildly erratic depending on a company's product category, the week, and the location.

Businesses worldwide that had been wading through waves of chaos have entered into a deeper chamber of uncertainty. What has become certain: The world economy is in various stages of pause; the question is not when will the world be back to the previous reality, but what will the new reality be. In this new era, future success will require an entirely different modus operandi.

Managing a standard crisis is all about executing contingency plans that have been well considered. But managing a crisis of this magnitude is about overhauling the operating system of your company to be able to deal with the unthinkable and, as a consequence, the unplannable. At the most basic level, the pandemic has taught the world that during times of crisis, business as usual must be tossed out the window in favor of contingency operations to support acute resilience and agility.

Managing the Next 6-9 Months: The World Is Different

With uncertainty still taking its course, the health of global commerce and trade will depend on what kind of economic shockwave rolls out across the geographic regions. Its depth will be highly dependent on multiple factors, including consumer confidence and the reaction of public authorities.

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The implications are already palpable for businesses, consumers, and state governments. California, for instance, which amounts to the world's sixth largest economy, has watched the pandemic drain its heralded $21 billion budget surplus. Projections estimate that COVID-19 will drag it into deficit—to the tune of about $55 billion—and drive the unemployment rate to 18% as retail, tourism, and restaurants suffer.

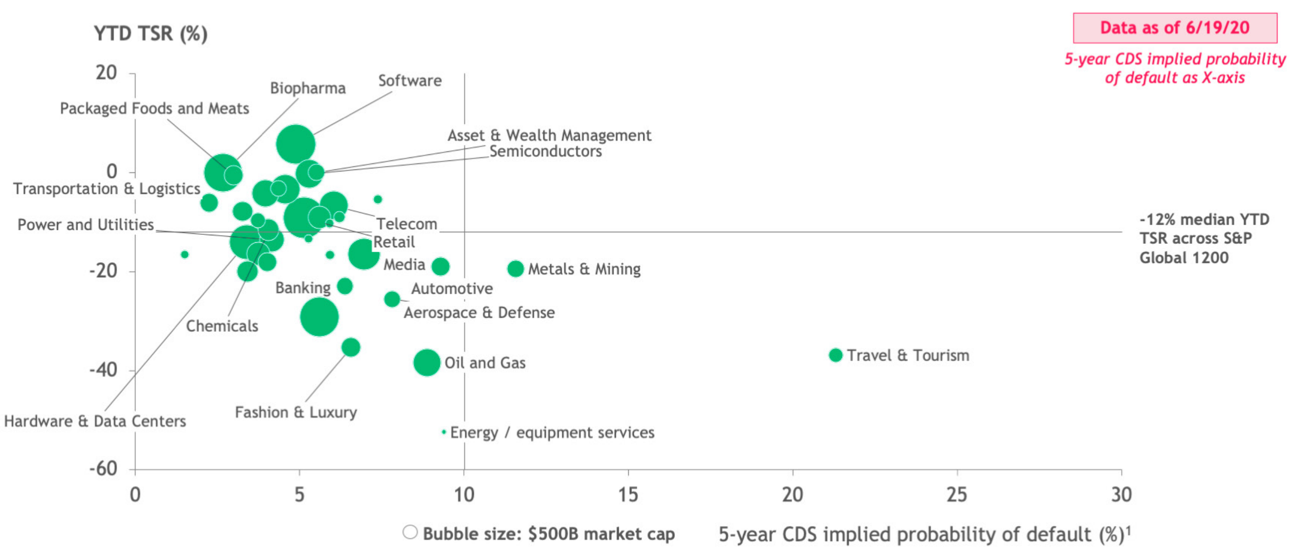
While the lion's share of layoffs has likely already occurred, as bleak government data emerges, the ensuing domino effect may lead to additional layoffs; and already-lean budgets will become even tighter. Companies will need to take a closer look at structural cost cutting. In the world of commerce, this translates into even more challenges around demand, like avoiding stockouts, dealing with order cancellations, and managing SKU changes. Not only will demand evolve but also consumption patterns. The foreseeable surge of e-commerce is one of them, creating challenges for supply chains from specific storage needs to last mile delivery.

Another interesting lens: the prospect of new health and safety rules, lifestyle habits, and product preferences as a result of the COVID-19 experience. Businesses will need to reconfigure workspaces, likely with different types of equipment and products than before to maintain safe distances and hygiene. Restaurants, public transit, and entertainment venues will also follow suit. And, if people choose to avoid public transit, what will they turn to instead?

Cars? Bikes? More forms of exercise that would drive a surge in different types of shoes or athletic wear?

According to one BCG study, 40-60% of respondents in the US, China, and Western Europe said they will use public transit less or much less frequently, choosing walking, biking, or driving their own cars, instead—at least for the short term. Meanwhile, bike sales have already taken off in the US, as findings from the survey report: "Sales of bikes, related equipment, and repair services almost doubled in March compared with the same period in 2019. British Cycling, an advocacy group, estimates that COVID-19 might prompt some 14 million Britons to choose a bike over a car, according to the World Economic Forum's COVID Action Platform.

Overall sector view: O&G and Travel & Tourism particularly vulnerable



1. Function of sector median 5-year CDS spread and credit ratings - signifies default probability within next 5 years
Note: CDS spreads were used for insurance in the place of Net Debt/EV because their debt positions are inherently different than all other industries; medians approximated by companies in S&P 1500 and S&P Global 1200
Source: S&P CapitalIQ, BCG analysis

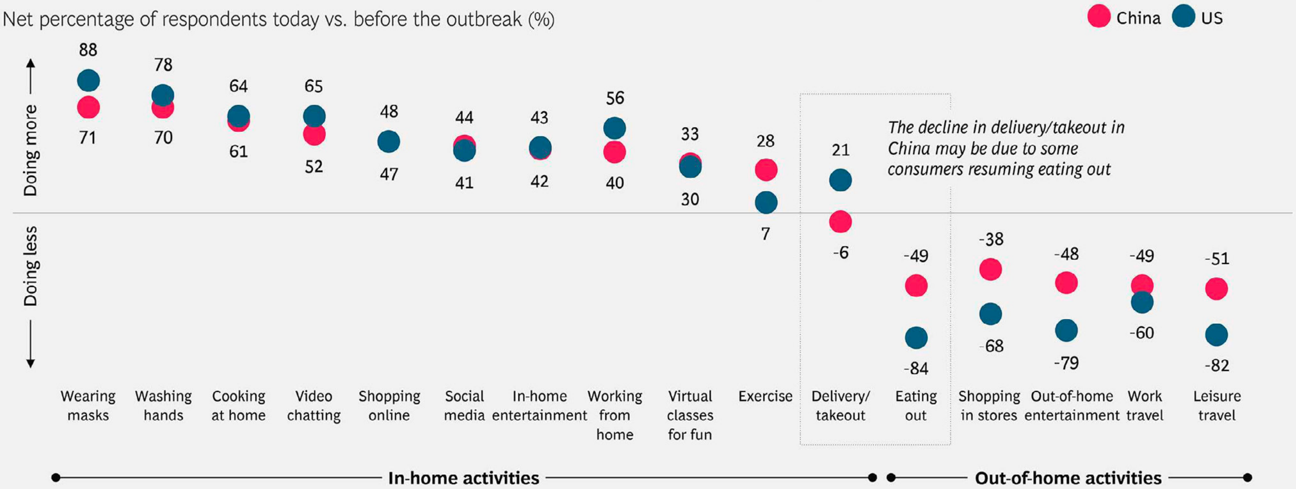
GLOBAL – WEEK 12 – MAY 22–25

Exhibit 2 | More Chinese Consumers Than US Consumers Are Resuming Out-of-Home Activities; In-Home Activity Levels Are Quite Similar

China's in-home activity levels remain elevated and similar to the US's…

…while its out-of-home activity levels show a positive rebound

Net percentage of respondents today vs. before the outbreak (%)



Source: BCG COVID-19 Consumer Sentiment Survey, May 22–25, 2020 (N = 3,238 US; 2,963 China), unweighted, representative within ±3% of US census or China national demographics.
Note: Question text: "Which of the following best describes how your behavior across the following activities has changed due to the coronavirus?"

In May 2020, BCG's Center for Consumer Insight conducted a survey in the US and in China, asking how behavior across several activities had changed due to the Coronavirus. Even though China's pandemic recovery had an earlier start than the US, behaviors in both countries appeared to be similar. A return to regular activities from prior to the outbreak seemed to be sluggish in China, not to mention elsewhere.

Although consumers were starting to resume out-of-home activities, the areas of focus that had previously soared in their replacement were waning. As eating out increased, for instance, delivery and takeout started to drop. Even still, the rediscovery of digital conveniences will likely continue to support the takeout and delivery model. What is safe to believe is that the epidemic will be ongoing; hot zones might erupt in some areas in the coming months while a form of normalcy returns in others. With that, some countries will likely be opening as others find themselves shutting down; leisure and even business travel will be limited or nonexistent. The theme of unpredictability will continue as society wrestles with serious judgment calls:

- What will be the safety metrics for going back to work?
- How will businesses gear up to apply proper health and safety measures for their workforce?
- How will industries ramp up and find the sweet spot for the right amount of inventory to carry?

These questions will have meaningful impact on supply chains.

A Fresh Approach in a New Era

To remain viable, companies will need to keep a constant finger on the pulse of what is current in their worlds around demand and transport capacity. And, understanding overseas suppliers and their dependencies will be just as important.

> **When goods are held up, businesses are risking the wrath of unhappy customers, while working capital is stuck in transit...**

For instance, if a company moves its production capacity from South China to Vietnam— impacting its supply chain—it's important to know how this will affect cost and on-time performance. Tariffs, labor, and IMO fuel charges all come into play on the cost side.

In April 2020, for example, the ocean market saw many service cancellations on the Transpacific trade lane, with an average of nearly 20% of all sailings taken out of capacity—and reaching as high as 28% during the last week of the month. And, despite the air market improving slightly, the capacity loss was still floating around the 20% to 25% mark. "It's understandable that, during a disruptive time, carriers need to make adjustments to protect their solvency. But at the same time, businesses need greater certainty and predictability to be able to plan and forecast. It's a very real dilemma," notes Sanne Manders, Flexport Chief Operating Officer.

> Being able to switch supply chain solutions on the fly will be critical.

When goods are held up, businesses are risking the wrath of unhappy customers, while working capital is stuck in transit—further testing budgetary resilience. Being able to switch supply chain solutions on the fly will be critical.

With conditions more dynamic than ever, businesses will need to watch for shifting sands in the form of increasing—or decreasing—consumption. It is no longer about having a Plan B, but Plans B, C, D, E, F, and G. In other words: being adaptive.

A Two-Stage Plan to Emerge from Disruption

Looking ahead, one thing is certain: Knowing transport options and having flexible operations will allow for fast response as the market shifts again and begins to ramp up. Just as cyclists crank down a hill to carry the momentum into an uphill, businesses need to have conditions in place to head out of the downturn. And, control and visibility are essential.

To prepare for the post-COVID-19 reality, Flexport and BCG suggest the following:

1. Near-Term: Navigate through the Crisis and Prepare for Recovery
    a. Proactively adjust your supply chain to protect the business from cost increases and slipped production or delivery schedules.
    b. Build scenarios for ramp-up and take stock of how best to use your resources: employees, available assets, and emergency transportation solutions.

2. Medium-Term: Grow Out of the Crisis
    a. Assess how the company has weathered the disruption and look for opportunities to improve.
    b. Prepare for new potential disruptions by putting supply chain tools in place that provide control and visibility.
    c. Understand the new reality and rethink your strategy in view of new consumption patterns, operational constraints, and all critical stakeholders, from employees to suppliers.

The Post-COVID-19 Era: Learning from the Crisis

In 1997, Toyota learned an invaluable—and painful—lesson in resilience. Operating on an efficient business model referred to as "just in time" production, the company sourced the exact volume of parts needed for the specific number of vehicles waiting to be assembled. One specific part, a P-valve, was manufactured by a single supplier that produced nearly 33,000 valves daily. But when a fire broke out at the factory, the production line that made the part was incinerated. As The New Yorker put it, "The fire had now put the whole enterprise at risk: with no inventory in the warehouse, there were only enough valves to last a single day. The production of all Toyota vehicles was about to grind to a halt."

> **"The silver lining in massive disruptions is the learning opportunity...**

In response, the company quickly reached out to a number of factories, regardless of whether or not they had a prior relationship to Toyota or the industry. Using detailed manufacturing instructions, the factories transformed their operations to produce the essential part to help save Toyota. Lesson learned: De-risking relies on redundancy, diversification, and key partnerships. It's not hard to imagine that this case study inspired companies like Dyson, Ford, and GE to switch up operations to help fill the void of PPE during the pandemic.

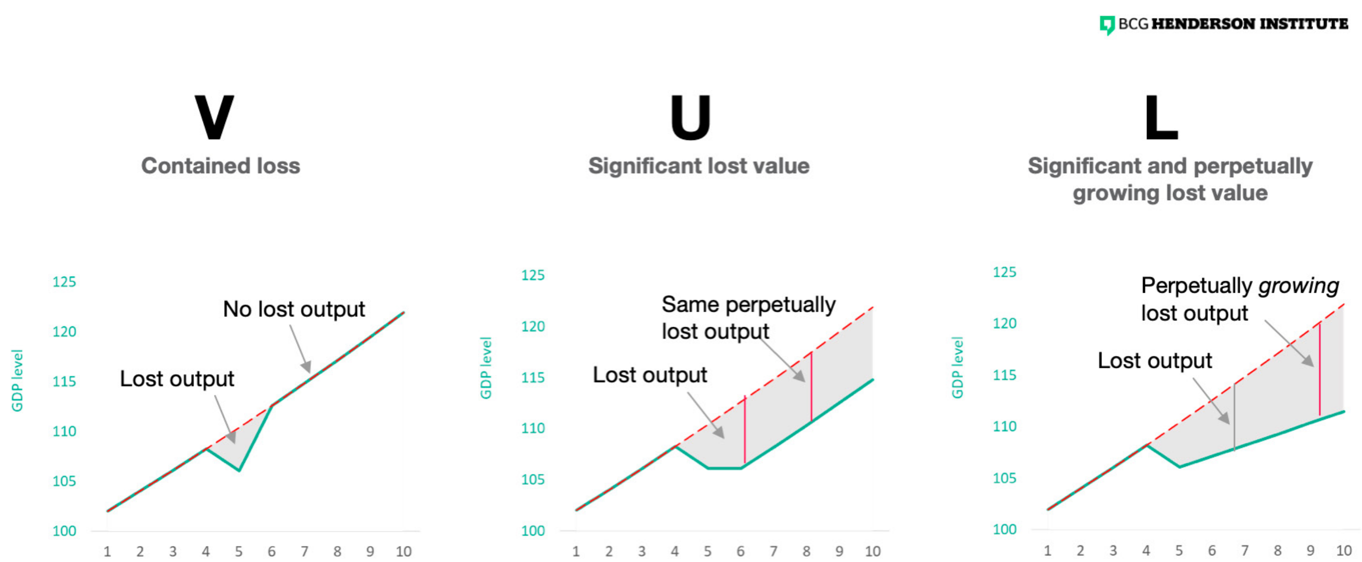
The silver lining in massive disruptions is the learning opportunity. For global trade, it presents a strategic opportunity to optimize supply chains for greater resilience and agility to create a disruption-proof infrastructure.

Perhaps nothing is more important than to fully recognize that the world as we have known it has changed and now requires a different mindset, specifically with regard to planning and strategy.

Lesson 1: There's No Going Back to Normal

The pandemic has had a profound impact on consumption patterns. While it remains to be seen which ones will be fleeting, some are here to stay. With that, one of the most critical efforts a business can engage in now is to assess what the new reality will be, along with the risks and opportunities they will be facing as a consequence. Businesses and governments have moved into action to minimize the fallout. The outcome of these efforts will influence the economic recovery—and which shape it takes.

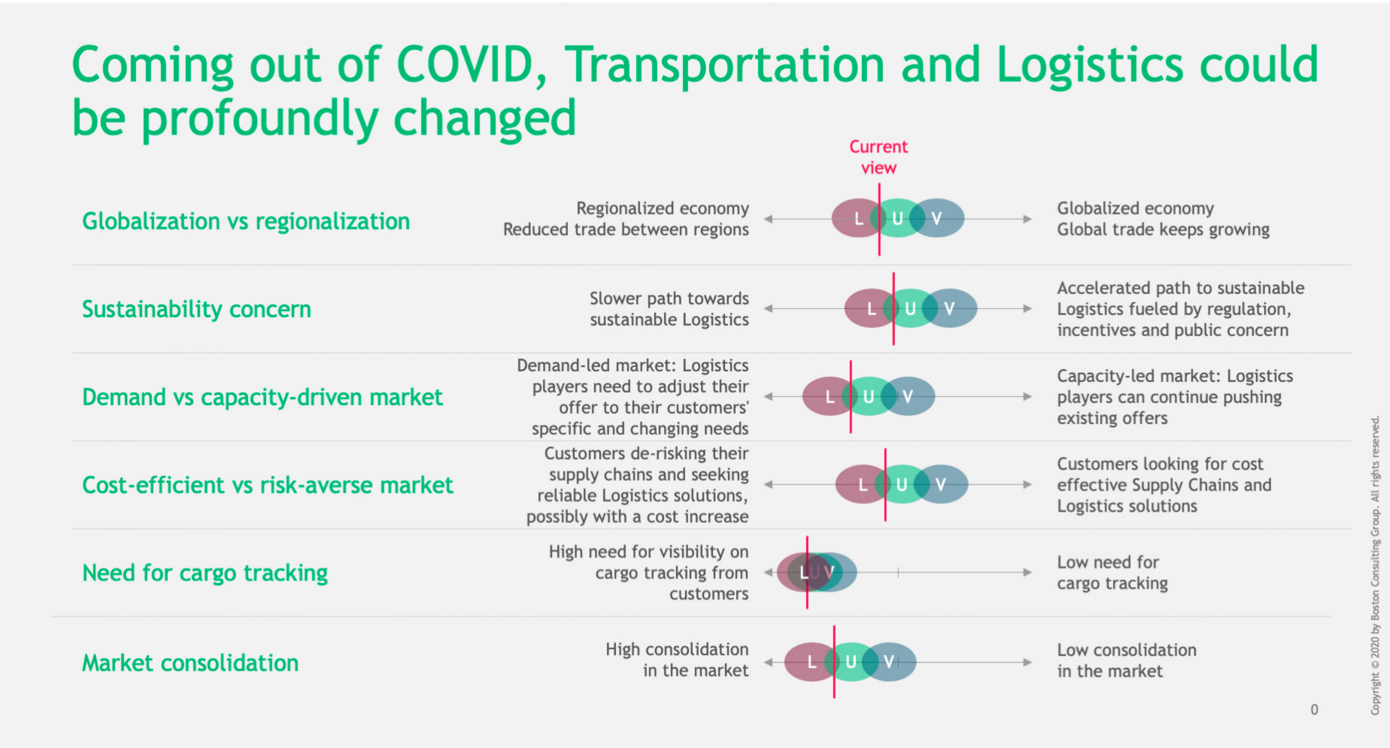
Different Economic Recoveries Possible



- In a V-shaped scenario, we can expect to see a dramatic dip with limited loss, followed by a sharp reboot that returns the economy to the previous trajectory.
- In a U-shaped scenario, the curve initially follows the steep dip of the V scenario, but with a slightly prolonged stall before resuming the recovery slope, resulting in some degree of unrecoverable loss.
- The more pessimistic L-shaped scenario, however, reflects deeper negative impact. In this scenario, the economy drops off, with a delayed return that is not able to resume the same upward trend as the previous scenarios. On top of that, there's no compensating for

the earlier loss and the follow-on growth path is markedly slower than before—typically triggering economic crisis.

Six megatrends are shaping the transportation and logistics industry, as shown in the exhibit below.



“In April 2020, we saw a small V-shaped recovery taking shape globally, but one that had a number of indicators that the countdown to ‘normal’ was going to be much more than just a few weeks,” notes Camille Egloff, Managing Director and Senior Partner for BCG. “Months later, the disease and economy trajectory are still highly uncertain and it is clear that there won’t be a ‘return to normal’ as such. From a sustainability standpoint, in the event of an L recovery, there could be a risk that climate and sustainability concerns are deprioritized and become the virus’s next victim. This could have long-lasting consequences for our lives and economies, and leaders should make sure that this doesn’t happen. A V recovery, on the other hand, will likely spark an accelerated path to sustainable transportation and logistics.”

The true effect of these megatrends will largely depend on the depth of economic disruption.

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As the so-called retail apocalypse swallows more businesses that brands rely on for distribution, they will be negatively impacted by fewer channels to reach customers.

When push comes to shove, businesses will need to reconnect with their corporate missions and devise a leaner operating model that incorporates integrated services with specifically chosen supply chain partners that share the same values.

Lesson 2: Agility Is the Name of the Game

Evolution is about adapting to be able to handle future uncertainties based on past experiences. Following are five key approaches to de-risk supply chain management in the face of massive disruption.

1. **Factor uncertainty into bid season**
   In the world of global trade, bid season is rife with opportunity to get ahead of the game or be relegated to the back of the pack. Much depends on when and how businesses lock in contract rates and what's included in the fine print. Those who understand what to look out for are often rewarded with competitive rates that deliver to expectations.

2. **Understand transport options to balance speed and budget with circumstances**
   Typically, most organizations will choose to ship by ocean to avoid the expense of air or to slow delivery if demand is flat. But certain times warrant the use of air, such as during holiday rush or when products are tied to time-sensitive events.

For those who choose ocean, knowing your company's needs regarding cost and time is everything. In the world of ocean freight, businesses pay for speed or space. Be clear on your corporate priorities. And, consider options, such as switching from classic ocean shipping toward multimodal solutions that combine air, rail, and trucking to move through disruption.

3. Conduct due diligence with your vendors

Whether it's a supplier or a carrier, the cardinal rule of supply chain management is to know what you sign up for. On the supplier side, it's wise to apply the same judgment as you might in real life: If it sounds too good to be true, perhaps it's not so good, after all. Ask vendors how they collaborate across functions and across other companies; how do they problem solve to ensure your products reach stores—and customers? Do they have redundancy built into their operations?

From a carrier standpoint, make sure rates come with space and equipment guarantees, even if circumstances go awry. Know what your contract says and what rates are based on. If a rate is especially competitive, make sure it's not at the expense of a much slower transit time that can trap your working capital in the process.

Verify that your vendors have business continuity plans in place to keep operations running. Are employees, including customs brokers, equipped to work from home? Are the warehouses open and able to store or stage freight?

Check business partners' financial solvency. Determine if a business partner is at risk for bankruptcy by looking at profitability, leverage, liquidity, solvency, and activity ratios.

4. Focus on technologies and forecasting

Key to achieving better control and more accurate forecasting is transparency with the entire supply chain process. For that to happen, technology and data must be in place. The right technology platform should bring all of a business' supply chain partners together to provide shared insights and updates. Doing so allows trends and patterns to emerge for smarter—and quicker—business decisions on the go. In addition, rich data informs future shipments for better control of supply and demand, as well as understanding landed costs of shipments.

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Moreover, technology provides visibility to help track where containers are and what's inside, down to the SKU level. By bringing labor-intensive processes into a digital platform, purchase orders and other important documents become much simpler to manage and collaboration takes place in real time, drastically reducing tedious emails and eliminating chances of error.

Also, stay current with global economic indicators, to help peg market predictions while filtering out the red herrings. Be aware of manufacturing shifts that can cause supply and demand imbalances.

5. Take advantage of supply chain strategies for risk reduction

Knowing how and when to speed up shipments can be advantageous in the face of uncertain supply and demand. For products that are likely to fly off the shelves at a given time, it's best to accelerate delivery. However, for goods that aren't selling, it makes sense to keep them at sea for as long as possible.

When choosing speed, premium or guaranteed services can provide greater control amid unpredictability. Premium services involve shipments through smaller vessels or faster boats, allowing for faster discharge that's then put onto premium rail. Guaranteed means shippers don't need to worry that equipment will be unavailable or that there might be blank sailings. Whatever is needed to get goods to their destination—ships, containers, chassis—will be committed.

When companies opt for slower shipments, it's vital to look at demurrage and detention fees in advance, to help guide the decision. Slow boats can be a good option. But in addition, some carriers offer 'suspension of transit' or 'delay in transit' options, which drop your container at a transit point that has lower demurrage and detention fees until the business is ready for final delivery.

> "The longer goods remain in transit, the longer it will take to recoup manufacturing costs and investment in inventory.

One important consideration when weighing the pros and cons of fast versus slow is the effect on working capital. Remember: The longer goods remain in transit, the longer it will take to recoup manufacturing costs and investment in inventory. To offset the waiting game, especially during times of disruption, stay in the know about government loan programs and other sources of funding.

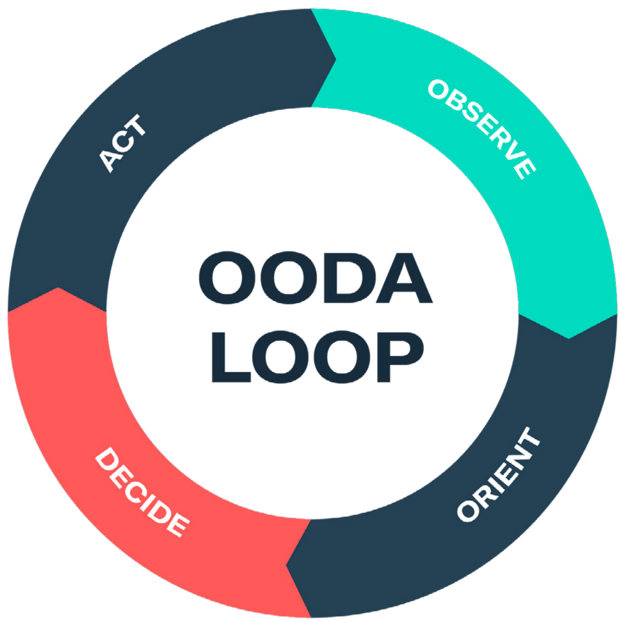
In the United States, for instance, SBA loans have helped small businesses cover payroll, get compensation for hardship related to disaster, and in some cases, provide debt relief. Similar programs have also been offered in the EU. Flexport helps customers get these loans and can also provide trade financing in some cases.

Lesson 3: Cultivate Agility to Speed Up Decision-Making

As businesses reconfigure operations to ready themselves for future disruption, failing to address internal culture can be a dangerous oversight. One model that provides a good framework to help develop agility—which Flexport follows—is a military concept called the OODA loop. The acronym stands for Observe, Orient, Decide, and Act.

Breaking it down, the first **O**, **Observe**, calls for examining priorities and urgencies. Is your company organizing around saving money or making sure products are on the shelf? Understanding how the organization is primed to perform in relation to its objectives is critical.

For instance, businesses that might go with the least expensive freight forwarder may not realize that one that provides in-house customs broker advisory services can help them find ways to mitigate tariff impact, avoid customs delays, and get products into market more quickly.



Orient, **the second O**, is about understanding market considerations to determine everything from manufacturing needs to the best way to move goods from origin to destination. This is where technology and the data within the platform can help guide informed decision-making—leading to the **D**, **for Decide**.

The last letter in the acronym, **A**, **for Act**, comes down to empowerment in order to take action. By removing layers of bureaucracy, those who are closer to the action are able to move quickly and effectively. For instance, at Flexport, businesses are assigned teams that comprise dedicated consultants specialized in various aspects of global trade. Team members are empowered to take actions necessary to ensure customers are able to keep the supply chain moving with maximum agility.

Summary

Building a strong company for the ages does not just rely on money in the bank and a strong portfolio of customers. As we've seen in the past few years, major brands have gone under due to an inability to weather storms like trade wars, shifting market conditions, and major disruptions like COVID-19. Surviving and thriving amid chaos and unexpected events requires agility and resilience baked into the corporate DNA.

To prepare your company for the next major disruption, keep in mind the following guidelines:

- **Resilience.** Don't over-rotate on the side of efficiency at the expense of resilience. Be sure to allow for backup options should the unexpected arise.
- **Diversification.** Remember that most successful operations are carried on the shoulders of many. When it comes to suppliers, think in terms of diverse players who can enrich your supply chain solutions.
- **Foresight.** Develop contingency scenarios for all possible disruptions and be ready to implement them. Leave nothing to chance.
- **Partners.** Know their values, capabilities, and operational approach. Consider that your brand's reputation relies on them. Make sure they're worthy.
- **Technology.** In supply chain management, visibility is everything. Use tools that can create easy workstreams for collaboration to increase transparency. Look for ways to mine data to drive business strategy.

Additional Resources

- BCG Infographic
- RFP Template
- Duty Calculator
- Forecasting Checklist
- Talk to an Expert

About Flexport

Flexport is the modern freight forwarder. Companies use Flexport to move freight, clear customs, and make smarter decisions about their supply chain—all on one digital platform powered by a unique combination of technology, logistics infrastructure, and expertise. Today Flexport connects almost 10,000 clients and suppliers across 116 countries, including established global brands as well as emerging innovators. Flexport offers a full range of services, including ocean, air, truck and rail freight, drayage and cartage, warehousing, customs and trade advisory, financing, and insurance.

Learn more at flexport.com

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Boston Consulting Group partners with leaders in business and society to tackle their most important challenges and capture their greatest opportunities. BCG was the pioneer in business strategy when it was founded in 1963. Today, we help clients with total transformation—inspiring complex change, enabling organizations to grow, building competitive advantage, and driving bottom-line impact. To succeed, organizations must blend digital and human capabilities. Our diverse, global teams bring deep industry and functional expertise and a range of perspectives to spark change. BCG delivers solutions through leading-edge management consulting along with technology and design, corporate and digital ventures—and business purpose. We work in a uniquely collaborative model across the firm and throughout all levels of the client organization, generating results that allow our clients to thrive.