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Supply chain considerations from the conflict in Ukraine

How to stay on top of your supply chain.

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With economic hangovers and fragmented policy approaches to the pandemic already impacting business around the world, the conflict in Ukraine has only accelerated the need for businesses to think about the short- and longer-term supply chain implications. This crisis is another example of the continuous disruption to global supply chains, and businesses are looking to protect themselves against their exposures.

Many organizations are lacking the supply chain visibility, planning maturity, governance, people and real-time analytics to facilitate supply chain risk management and drive resiliency while balancing cost, agility and service.

So how should businesses seek to build resilience into their supply chains moving forward? Below are some of the considerations to help build resilience and agility in your supply chains.

Reputational damage

The room for businesses to be apolitical seems to be shrinking. Businesses are responding to calls to provide humanitarian support and disassociate themselves from entities that are contributing to the crisis. Even beyond the crisis in Ukraine, we believe that ideological, cultural and political rifts across and within nations are forcing businesses to make difficult choices that may make or break market development opportunities.

What you can do

- Understand relevant supplier tiers and respective sourcing arrangements to help mitigate the risk of exposure further up and down a business's supply chain. Being aware of risks enables proactive management.
- Be transparent about a supply chain ecosystem of partners so all stakeholders and consumers have visibility into where products are from or where services are conducted — and this goes beyond Tier 1 and 2 suppliers. Reassuring all trading partners, especially consumers, is paramount to help mitigate a dip in sales or the loss of consumer confidence.
- Build agility into operating models, which is likely only achieved when full value chain visibility and real-time analytics are embedded within the supply chain planning function. There's a need to react swiftly and be agile to help mitigate against relevant exposures.
- Hold true to the company's values. More than ever, businesses are testing their commitment to their values and the environmental, social and governance (ESG) agenda, especially as they prepare for and respond to geopolitical events.

Logistical disruption

Delays, cancellations, port omissions, infrastructure damage to delivery channels and elevated freight rates are impacting companies reliant on the global shipment of goods. Major logistics instability can affect the accuracy of supply chain planning and meeting customer needs along the value chain.

What you can do

- Assess which commodities or items may be an immediate challenge. Are there alternative sources, production changes or sourcing strategies (e.g. near-shore or on-shore alternatives) that can be made? These alternatives may be a little more expensive but can contribute toward a higher customer fulfilment experience.
- Diversify supply chain inputs. There are undoubtedly efficiencies associated with sourcing from a single supplier — but a sole-source supplier may also make the supply chain more sensitive to interruption. Supply diversification should be assessed, and alternative sourcing plans put in place.
- Consider restructuring supply chain flows in the longer term. A deeper trend toward regulatory fragmentation and interventionism — which started a few years ago and may be compounded by the crisis — is causing some companies to restructure supply chain flows.
- Don't assume a business can simply repeat what it has done in previous years in freight forwarder (FF) contract negotiations. The FF industry is being challenged, where certain FFs may have a hard time complying with new or upcoming delivery dates (even if a premium is paid) and may avoid entering into new contracts.

- Understand the true cost to serve, model the options and understand the impact on customer experience. Because while it may be more expensive to fly it, it can be worth it; the alternative (running out and not serving at all) may not be an option.

Increasing input costs

In our view, elevated prices for key inputs like oil, grain, machinery, steel and timber are creating a surge in global commodity prices, adding costs to doing business and affecting profitability. Inflationary pressure may also further accelerate the already developing trend of countries turning inward and prioritizing domestic industry in order to build resilience as part of their national strategic goals.

What you can do

- Consider M&A and joint venture opportunities. If the material is strategic and unique to a core product, explore the economics of a potential merger, acquisition, joint venture or stronger alliance/partnership with a more localized source of supply. These should be thought through early in a sourcing process and are part of a risk-mitigation balancing act — knowing you may not have the best price but have surety of supply.
- Review contract rights. For customer and supplier relationships that may be impacted, contracts can be reviewed to help identify whether the contracts contain a force majeure provision — and whether such clauses provide termination rights.
- Use contract negotiation levers like shorter payment terms in exchange for tempered commodity pricing or volume discounts to help incentivize suppliers.
- Analyze available data so short-term decisions can be prioritized and made swiftly.
- Consider the accelerating impact of "friend-sourcing", where businesses look for like-minded and "safe" investment and trade partners. This may be particularly the case for energy, given energy security's critical role in national security.

Resilience and supply chain continuity

In an uncertain environment, it can be even harder to predict the future — but understanding where supply chains are most vulnerable to external shocks is one of the first necessary steps to help build resilience. During the pandemic, many supply chains didn't stand up to the challenge, and the few that did were only resilient by incurring additional costs within the business.

What you can do

- Assess the geopolitical exposure of the supply chain. For example, identifying overreliance on politically volatile markets for key input products or commodities can encourage a supply diversification strategy, targeting more stable and alternative sources. (Consider if there are any "no-go zones", where the risk and chance of sanctions make it an area to avoid.)
- Consider sourcing alternative suppliers. Businesses may need to find alternative suppliers, and in some cases customers, in a way that limits legal and commercial exposure. These processes can add cost and increase lead times for delivery, affecting fulfilment and end-customer satisfaction. Strong procurement governance is crucial.
- Scenario-plan for potential events. Scenario planning helps improve business resilience, especially when enabled by real-time analytics and alerts. The goal is not to gauge *if* a disruption will happen but rather to shape action plans ready to deploy *when* adverse conditions arise. There's no one-size-fits-all approach; a company's response depends on variables like industry and geographical exposure.
- Think creatively in addressing supply chain disruption issues. Some forward-looking companies are starting to build strategies to mitigate the impact of second wave supply chain risks, thereby aiming to reduce shortages and redundancies of critical components and commodities.

Sanctions

Sanctions, restrictions, tariffs and embargoes can all result in additional costs that should be absorbed by businesses within their supply chains.

What you can do

- Keep track of all existing and upcoming sanctions to best assess the business impact. Monitoring and assessing the far-reaching implications of the broad suite of economic sanctions impacting Russian supply chains is paramount for future planning activities.

— Screen and automate. Easily adaptable screening and know-your-customer (KYC) automated tools are essential in this quickly developing sanctions environment. Even if the conflict is resolved in the span of a few months, sanctions and restrictions may remain in place long after.

— Consider forensic due diligence: It may be important to leverage forensic due diligence on third parties, fourth parties and beyond.

Cyber security in the supply chain

The conflict in Ukraine highlights the importance of understanding the security and resilience of all partners across the vital areas of supply chains — including upstream and downstream — to help reduce the threat of third-party risk exposures and attacks. Precautionary actions can include heightened network monitoring, drilling for cyber-attack scenarios, searching networks for threats and penetration testing, among other techniques.

What you can do

— Identify the dependencies on vendors and partners from Ukraine, Russia and neighboring countries and build a contingency plan should they be cut off from the supply chain.

— Increase the monitoring of network traffic from countries involved in the conflict — especially from critical suppliers — as cybercrime is expected to get more sophisticated, with many hacking groups having a free hand in the current situation.

— Understand the incident response and resilience planning critical suppliers (at a minimum) have put in place.

— Understand the impact of potential incidents in the supply chain on the business to determine where to focus increased monitoring and greater readiness to respond.

Next steps

The conflict in Ukraine is driving increased supply chain disruption and concerns for the resilience of critical business services. While the current climate is unpredictable, consider how the situation may develop over time and the scenarios that may arise.

1. Understand key exposures.
2. Determine available options and ramifications, including the longer-term view.
3. Prioritize and action any next steps.

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