

When you're overdue for scenario planning

The Law of Unintended Consequences has again played out on the world stage: Hong Kong's riots abruptly ended, CO2 emissions from mega-polluter China dropped dramatically as factories have gone dark, and even the upper atmosphere is cleaner, as first dozens, then hundreds, of gas-guzzling airline flights were canceled. And if you're in the facemask or hand sanitizer business, these are boom times.

So, if you guessed I'm talking about the coronavirus, you win.

It is a pandemic that has already disrupted the global economy and promises to further hinder trade. Supply lines for both raw materials and finished goods are being impacted. This pandemic is hobbling the world's second-largest economy, resulting in wild swings in the Dow and sending the 10-year Treasury yield to record lows.

But have you ever noticed that when something bad weighs down the economy, markets, the press and people overreact as if it's a first?

We're seeing this now: However, this is hardly a unique supply-line failure — it's just that too many in the business world have the memories of goldfish. What it is, though, is yet another reminder that for a business to survive any such extreme trade event, they need to think ahead.

That's because in the global economy, the supply chain pipeline is six to 12 months long in many cases, from placing an order for, let's say, the raw material you need to manufacture your product, to having it shipped from outer Mongolia, and then getting it from the shipping port to your factory.

So, you're bumping along thinking everything's fine, then suddenly you



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get a rude awakening — “Where’s my stuff?”

And nobody seems to know or be able to get a straight answer.

For example, say you get a significant percentage of components to manufacture your product from China. With plant shutdowns your lead time increases from what is typically four to six weeks to 15 weeks. Your options? You could pay more for components from alternative sources, but at what price?

However, if you can't get what you need elsewhere, you could be out of business. And if your competitor gets it from somewhere else because they saw the writing on the wall, they win.

Earlier disruptions

There have been notable cases where companies saw that writing, as happened after then relatively small Royal Dutch Shell created a geo-political-economic “scenario-planning” team that alerted Shell in advance to some of the biggest economic shocks to come, like the 1973 energy crisis, the severe price shock of 1979, the collapse of the oil market in 1986, and others. And that helped them thrive when the you-know-what hit the fan.

But those sorts of disruptions weren't unique either. Supply-chain failures happened to Britain, our largest trading partner, in the revolution, the

war of 1812, and the Civil War (when the Brits sided with the South). And it happened in 2015 after a union slowdown at West Coast ports that affected the whole country. And it has happened repeatedly when the UAW strikes.

All were cases involving one variable — getting access to your inventory. But if you can control that variable by planning for every contingency, then you may be OK. Can't find Diet Coke? Guess where the artificial sweetener comes from — yup, China.

Also, with this virus event, a lot of companies are paying the price for being too reliant on China. And many Western companies not yet chased out of China by rising labor costs and a massive and opaque bureaucracy may call it quits and move their factories elsewhere.

Some very large companies can soldier through such disruptions, of course. Walmart, for instance, just missed its fourth-quarter earnings after 120 of its stores in Chile were looted and some burned down, resulting in a \$110 million hit to operating income. But for Walmart, that's a blip. And Walmart isn't dependent on a single source or market for its hundreds of billions in sales.

In any case, this is a wake-up call for companies large and small. Ask yourself, who are my biggest suppliers and how can I replace them? And who are my biggest customers and how can I replace them?

That's right: You're overdue for some scenario planning.

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