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Moving from faster prediction to faster response in FMCG supply chains

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Executive summary

Fast-moving consumer goods—at least some of them—have become emblematic for 2020.

If there was ever any doubt about the importance of resilient supply chains in the fast-moving consumer goods (FMCG) sector, one need only recall the expanse of empty shelves that had once held toilet paper or pasta at the onset of the Covid-19 pandemic. In March, in the UK alone, there was “more than £1bn worth of food stocked in people’s houses than there was three weeks ago,” according to Helen Dickinson, chief executive officer of the British Retail Consortium.¹

While these events could not have been anticipated, they demonstrated the vulnerabilities within supply chains. Over the past three decades enterprises—not least in the FMCG sector—have become ever more global in their scope. Reducing slack in supply chains, along with inventories, has optimised cash flow and business returns. But the rise of protectionism over recent years had already been challenging this model, and in 2020 the sector was hit by a perfect storm of geopolitical instability, spiralling commodity prices and ratcheting tariffs, topped off with a global pandemic. This report gives an unrivalled insight into the challenges facing the sector—not only from the Covid-19 crisis—and how supply chain executives have been adapting.

Key findings include:

- **The Covid-19 catalyst:** FMCG companies have spent decades developing global supply chains and reducing inventories, thus optimising returns. The rise of protectionism had already been challenging this model before the coronavirus outbreak. The pandemic has simply accelerated what had already been brewing in the sector.
- **Growing concerns:** Of all the trends, the Covid pandemic has unsurprisingly had the largest impact, particularly in the US. Survey respondents were also concerned about major price fluctuations in commodities and global cyber-attacks, which were a particular concern for Europeans. US respondents highlighted territorial disputes in the South China Sea.
- **Near-sourcing is far-sighted:** The shortening of supply chains—or “near-sourcing”—has been a strategically important response to the year’s multifaceted crises. Regionally, near-sourcing was most important for both the Asia-Pacific region and Europe, while being considerably less so for US respondents.
- **Cost considerations are a regional issue:** Lowering costs is a more important consideration in the US and Europe than in Asia, where many economies, especially China, are instead looking for the better profit margins that can be achieved with more sophisticated products.
- **The growing importance of sustainability:** Labour conditions and wages are the most significant sustainability issue in our respondents’ supply chains, as companies tend to focus on their most prominent problem. However, the headline

¹ <https://publications.parliament.uk/pa/cm5801/cmselect/cmenvfru/263/26305.htm>

figure conceals a sizeable difference, as Europe and Asia rank labour issues much more highly than US respondents.

- **Resilience—can't pay, won't pay:** While the Covid crisis has demonstrated the importance of supply chain resilience, it

remains cost-constrained for most. FMCG businesses run on high volumes and low margins, with less room for manoeuvre in cost terms than in other sectors. Change will come through changing working patterns rather than increasing spending.

About this report:

To find out the main challenges affecting global supply chains, and what this might mean for the future of industries, The Economist Intelligence Unit, commissioned by Maersk, surveyed 450 supply-chain executives across three sector verticals (lifestyle, retail and fast-moving consumer goods) in seven countries—Australia, China, France, Germany, Japan, the UK and the US—spanning four continents. This report focuses on the FMCG industry. We would like to thank the following experts for their time and insight:

- Marco Querzoli, EMEA vice-president of supply chain, Kimberly-Clark
- Marcel Martin, group supply chain director, Coca-Cola HBC
- Chengyi Lin, affiliate professor of strategy, INSEAD.

The report was written by Dewi John and edited by Candice de Monts-Petit.

Introduction

Doing business—especially doing business globally—is becoming an increasingly fraught endeavour for our respondents, who are confronted not just by a pandemic but also by escalating trade disputes, regional conflicts, Brexit and a global economy that was slowing down well before the coronavirus struck.

Marco Querzoli, EMEA vice-president of supply chain at Kimberly-Clark, referred to this as “new types of challenges that had not really been considered before and not in combination. With Covid they hit all at once.”

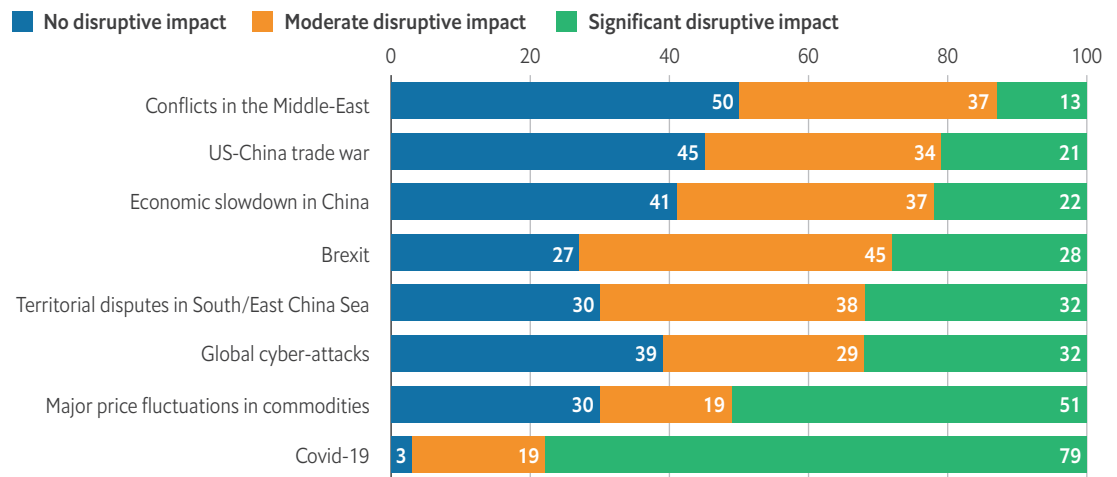
This report looks at how prepared FMCG businesses were for these effects, how they have withstood the impact so far, what measures they have taken to mitigate its effects, and how leading representatives of the FMCG sector see the experience changing the way in which they manage their supply chains.

Part I. What’s keeping FMCG procurement managers awake at night?

It is hardly surprising that Covid-19 has had the largest impact on FMCG supply chains, with 79% of respondents scoring it as “significantly disruptive”—in line with the global survey

average of 78%—and a further 19% scoring it as “moderately disruptive”. This was felt most strongly in the US (86%), and least strongly in Europe (69%).

Chart I. Impact of geopolitical events on FMCG supply chains (%)



Source: The Economist Intelligence Unit.

Percentages rounded up/down so total may not be 100%

The second most significantly disruptive event cited by our respondents was major price fluctuations in commodities, at 51% – six percentage points above the broader survey average. Global cyber-attacks came third at 32%, indicating the changing nature of businesses that are increasingly technology-dependent. This was matched by territorial disputes in the South/East China Sea (32%), with the latter mainly driven by US respondents (44%), which may indicate that the US has the most transcontinental FMCG supply chains and Europe the least at 16%.

While the English Channel may not have the breadth of the South China Sea, its disruption can still be highly problematic for those who are dependent on shipping goods across it. When adding up the response to significant impact (28%) and moderate impact (45%), Brexit was viewed as the second most impactful event (73%) after Covid-19 (98%). Unsurprisingly, nearly half of Europeans (44%) saw Brexit as a significant problem for their supply chains.

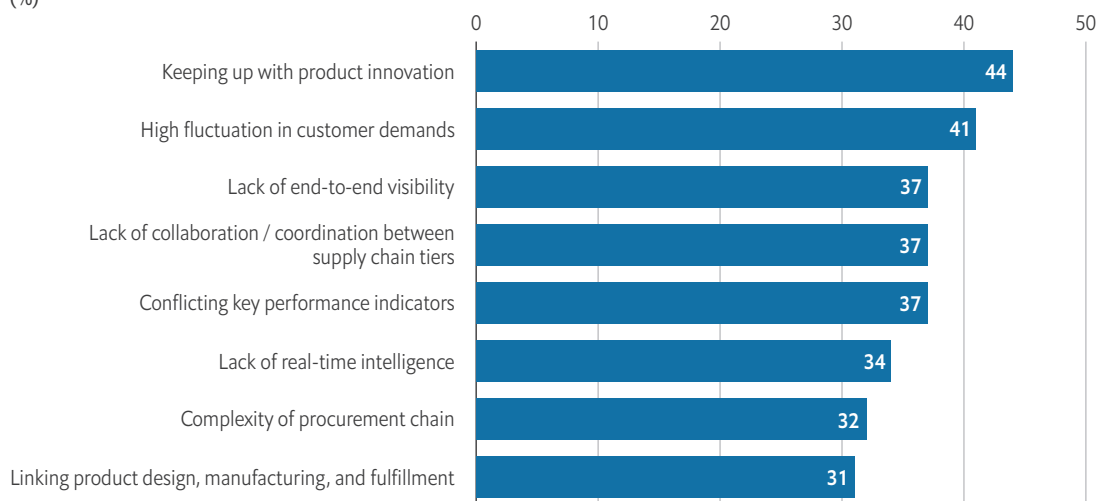
Geopolitical issues are only one facet, albeit an important one, of the challenges experienced



by FMCG supply chain executives. Asked about the biggest challenges they faced, respondents cited two issues inherent to the “fast-moving” nature of their business as their top concerns: keeping up with product innovation, which was chosen by close to half (44% globally, rising to 50% in Europe) of those surveyed, and high fluctuations in customer demand (41% globally, rising to 47% in Asia).

A lack of end-to-end visibility, lack of collaboration between supply chain tiers and conflicting key performance indicators were equally viewed as key challenges by over one-third (37%) of respondents. US-based executives were most concerned about supply chain tiers collaboration (cited by 53%), while conflicting indicators (43%) were the main concern for Asian ones.

Chart II. Main challenges that FMCG supply chains are facing (%)



Source: The Economist Intelligence Unit.

Part II. Gravity’s rainbow

There have been numerous debates about the importance of “gravity” in trade – in other words, is the pull of larger and nearer markets becoming stronger? To what extent are companies, if at all, narrowing their global scope and switching to a “near-sourcing” model?

Making major changes to their sourcing strategy in the form of near-sourcing was cited by FMCG respondents as the second most important strategic objective, with one-quarter flagging it, following improving traceability, at 29%. Although the process was in motion before Covid-19, it has been further catalysed by it and is therefore still very much in development.

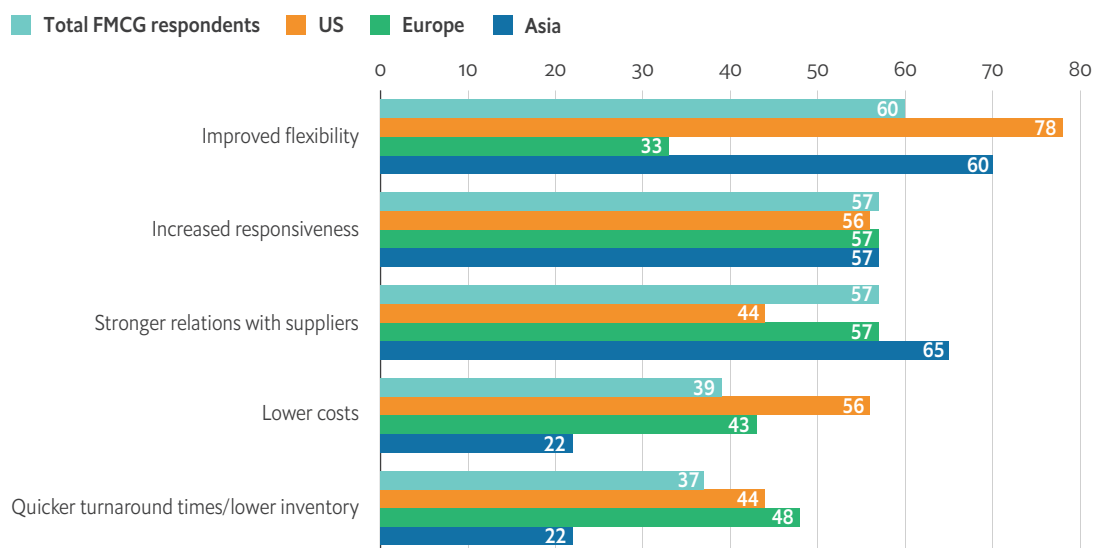
“We prioritise wherever possible local sourcing,” says Marcel Martin, group supply chain director at anchor bottling firm Coca-Cola HBC, who explains this is not something

that has been brought on by Covid-19 but is intrinsic to the nature of the business.

At the regional level, near-sourcing was most important for both Asia-Pacific and Europe, at 30% and 29% respectively, as opposed to the US, at 18%. The latter is perhaps surprising, considering the weight given to such issues as the geopolitical instability in the South China Sea.

The main advantages of near-sourcing were felt to be stronger relations with suppliers, improved flexibility and increased responsiveness – all of which came in at above 50%. However, this headline figure conceals significant regional disparities. Improved flexibility was very important for US (78%) and Asia (70%) respondents, but considerably less so for Europeans (33%), who instead prioritised increased responsiveness and stronger relations with suppliers (both 57%).

Chart III. Main benefits of developing a “near-sourcing” strategy
(%)



Source: The Economist Intelligence Unit.

Although a slightly less determining factor across all regions, lower costs, at 39%, were an important driver for respondents in the US (56%) and Europe (43%), although it was significantly less so for Asian respondents (22%), which possibly indicates that many of

its economies – not least China – are moving up the value chain and looking for the bigger margins that can be achieved with more sophisticated offerings rather than through squeezing costs further.

Part III. Innovating out of a crisis

Niccolò Machiavelli, the Italian Renaissance philosopher, is credited with coining the phrase “Never waste a good crisis”, and this certainly seems to apply to what has happened over the past year in the FMCG sector.

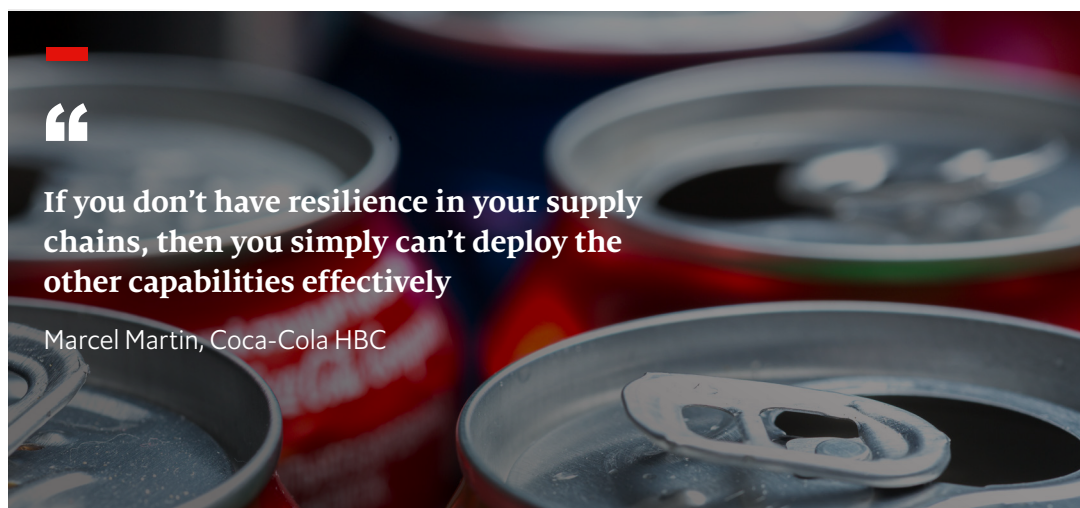
Chengyi Lin, affiliate professor of strategy at the graduate business school INSEAD, sees significant consumer trends influencing supply chains in the FMCG sector that have accelerated because of the Covid crisis. There are three principal components: a shift to digital, the increasing importance of sustainability, and a generational shift. “Covid has driven the integration of the digital experience and the reconfiguration of supply chains to increase their agility,” Mr Lin says. “The focus has shifted from faster prediction to faster response.”

This has also been the experience of Kimberly-Clark’s Mr Querzoli. “We already had a digitalisation programme in place, but Covid has sped up that process as we need more flexibility,” he says. The experience of the pandemic has developed the company’s thinking in areas such as robotics, which it had previously considered introducing with the

aim of “leveraging the use of new technologies wherever possible”.

Survey respondents outlined a broad range of technologies that are being used to enhance both resilience and flexibility, with averages across all regions ranging between 50% and 60%. Although a greater regional spread is evident, it is clear that FMCG firms are keen on introducing cutting-edge technologies into their supply chains. For example, 79% of Asia-Pacific respondents, a considerably higher percentage than their American and European peers, saw 5G technologies as having a potential impact on supply chain flexibility, while European respondents saw the same technology as playing a greater role in resilience.

Mr Martin believes that companies which adopt such a flexible approach have to be able to prioritise different capabilities in different situations. However, building resilience is key. “The Covid-19 pandemic and its continuing impact demonstrate that if you don’t have resilience, then you simply can’t deploy the other capabilities effectively, or sometimes not at all,” he says.



Coca-Cola HBC has invested in technology to help the firm capture, understand and apply big data and advanced analytics, plus machine-learning algorithms for demand forecasting, which “have given the company greater end-to-end visibility across the supply chain”.

Mr Querzoli emphasises the importance of agility – which he defines as encompassing efficiency, speed and flexibility – to respond quickly to changes in the market. “We had been working three years to build our network, partnering with third-party logistics and working with our suppliers to secure our supply chain end to end. And, of course, doing all of this while optimising cost,” he says.

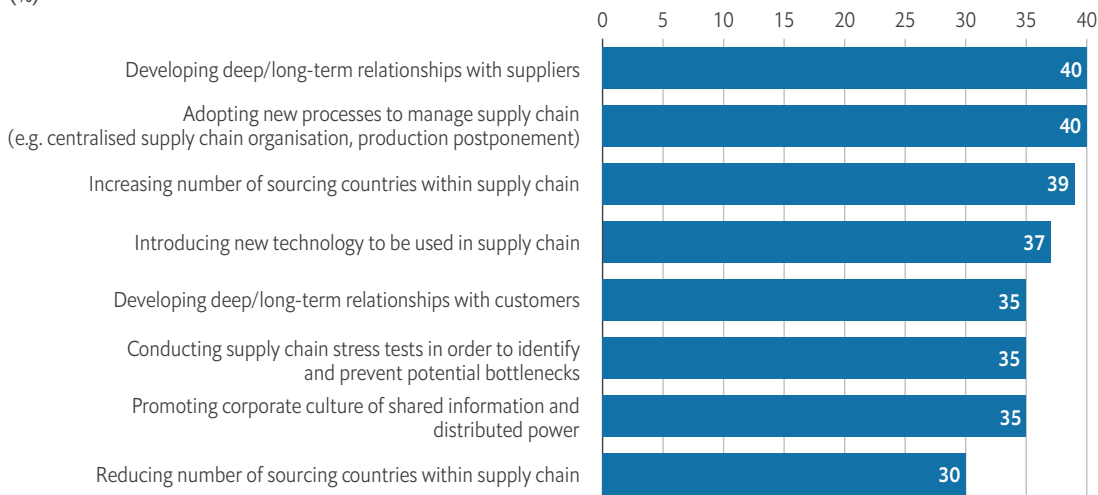
Nevertheless, only 20% of respondents believed that building resilience was a main strategic objective for their organisation’s supply chain. Indeed, 69% of respondents felt that the costs of making supply chains resilient

outweighed potential advantages. This was most strongly felt in the US, where 78% of respondents expressed this view.

The most popular way of achieving supply chain resilience has been the adoption of new processes, such as centralised organisation and production postponement, and developing deeper relationships with suppliers (both 40%), along with increasing the number of countries within the supply chain (39%). In contrast, 30% of respondents were looking to reduce that number, and this share fell as low as 19% in Asia.

Interestingly, more than 50% of US-based executives – the highest single result in response to this question – said they were looking to introduce new technologies, perhaps indicating less of a cost constraint in this region, at least in terms of short- to medium-term spend.

Chart IV. Measures implemented to build resilience in supply chains
(%)



Source: The Economist Intelligence Unit.

Part III. The impact of sustainability

Sustainability has been a hot-button topic that has continued to grow in importance over the past few years, with governments, regulators and investors placing companies’ social and environmental standards under increasing scrutiny. Rather than neglecting these issues to concentrate on the business of day-to-day survival, the coronavirus pandemic seems to have brought them further to the fore.

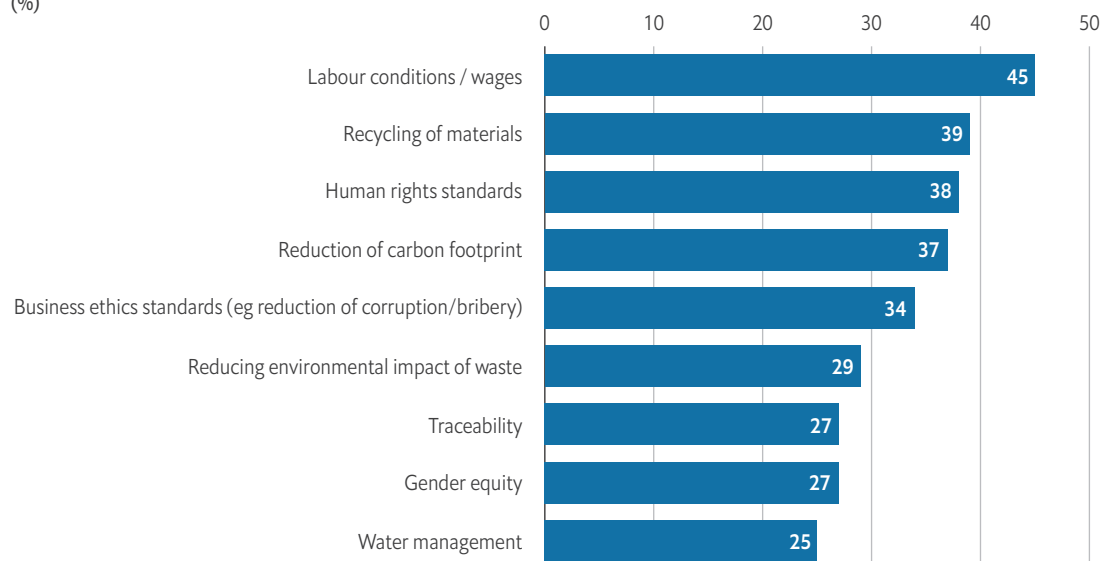
There is a wider spread in the responses to the issue of sustainability than was the case with resilience and flexibility, above. The survey ranked labour conditions and wages as the most significant sustainability issue within FMCG supply chains. “Companies tend to focus on their most prominent problem – for instance, with FMCGs, labour, working conditions and the use of child labour,” says Mr Lin. This is influenced by the fact that

“shareholders, not just activist ones, are increasingly demanding to know where the product is coming from.” Mr Lin cites the example of the Japanese market, where “in the organic section you see a picture of the farmer next to the produce – we’re not there yet with FMCG.”

The headline figure conceals a sizeable difference between how labour issues are ranked by Europe and Asia (50% and 51%, respectively), and the US (35%). Nevertheless, 44% of US respondents and 47% of Asia-based ones attributed a greater importance to the inextricably linked issue of human rights – something which Europeans (23%) scored significantly lower.

Traceability (27%) was a relatively low concern when it came to improving sustainability,

Chart V. Priorities in improving sustainability of supply chain
(%)



Source: The Economist Intelligence Unit.



Shareholders, not just activist ones, are increasingly demanding to know where the product is coming from

Chengyi Lin, INSEAD



although improving traceability was the sector's most frequently cited strategic objective. This may indicate that companies have started to implement successful traceability-boosting measures. According to Mr Lin, there has been a lot of innovation going on in different parts of the supply chain to improve this factor, although "this is at an early stage – nobody has the gold standard."

Mr Querzoli sees sustainability and safety, both with regard to his company's products and for its employees, as a fundamental issue throughout the supply chain. Such sustainability, he says, is "driven by the consumer but also by employee expectations," echoing Mr Lin's comments on the heightened importance of consumer pressures as an industry driver.

Kimberly-Clark is working on implementing sustainability measures, such as reducing its carbon footprint, increasing transparency, shifting to natural organic products, recycling, water and energy efficiency, and using more renewable energy – "really looking 360

degrees to figure out what is possible," Mr Querzoli says.

With regard to the sourcing of materials for his company's tissues, he says they have policies in place to ensure that they only work with "certified suppliers, protecting forests as much as we can to reduce our carbon footprint." That entails product transport "using lorries with next-generation engines" and also encompasses product design.

The sector, in parallel with other industries, is starting to focus not just on the immediate social and environmental impacts of their activities, but also on how these cascades throughout the value chain. "Meaningful work is starting on tracking total impact – CO2 emissions, water use, pollution and the like – not just of the product through the supply chain but after sale," says Mr Lin. This draws on nascent technologies which are able to provide crucial information on the activities of suppliers, such as monitoring social media for evidence of labour issues, or satellite images to monitor deforestation or soil degradation.

Conclusion: Where next?

The crisis generated by the ongoing Covid pandemic has speeded up the adoption of nascent technologies and working methods that were in development – from the ubiquitous uptake of video-conferencing to the implementation of less obvious ones, such as satellite imaging.

The shift in the role of technology from “faster prediction to faster response,” in Mr Lin’s words, means that futurology has, in a sense, become a new facet of FMCG supply chain management.

“Connectivity based on augmented and virtual reality will be critical and allow us to react fast to any kind of disruption, combined with robotics and automated vehicles,” says Mr Martin. However, he adds that the biggest impact will come from “the creation of a truly end-to-end digital ecosystem in our supply chain, which will strengthen planning, visibility and partnerships with our suppliers, logistics providers and equipment manufacturers.”

Nevertheless, he notes that “it is impossible to build resilience without people,” who will remain central to the implementation of any strategy. One feature of the issue of resilience

is that it remains cost-constrained for most respondents, even during a year in which the robustness of supply chains has been tested to its limits, and sometimes beyond. The FMCG sector is, however, a high-volume and low-margin business, and thus allows less wiggle room in terms of cost than other sectors. Primarily for this sector, then, change will be achieved through reconfiguring working patterns rather than increasing spending.

Most importantly, the experience of working through the Covid pandemic will put those businesses that emerge from it on a sounder footing for the other challenges they face. As Mr Querzoli says: “Managing the impact of Brexit should now be easier because Covid sped up that preparation.”

While no-one in this industry saw Covid coming, let alone wanted it, it has catalysed the greater uptake of technologies and a shortening and diversifying of supply chains that will engrain the lessons of this challenge in preparation for future ones. Or, in the words of German philosopher Friedrich Nietzsche: “What doesn’t kill you, makes you stronger.” Something of a motto for FMCG companies in 2020 perhaps?



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