

BRIEF 2

Supply Chain Security in Uncertain Times

QUESTIONS A BOARD SHOULD ASK

MAY 2021

Preface

Chartered Professional Accountants of Canada (CPA Canada) commissioned this brief to assist boards of directors in their oversight of company efforts to evaluate and reinforce supply chain resilience in the wake of major disruptions such as the global COVID-19 pandemic.

Every disruption brings its own lessons in the prevention, detection, recovery and response to risk and its cascading impacts. While no two risks are the same, proactive steps can be taken to buffer against the critical unknowns to come. Our discussion of supply chain resilience presents questions and commentary to support management and the board in driving shared understanding of:

- Potential vulnerabilities to stressors across the organization
- The potential impacts of such vulnerabilities on company sustainability
- Management's ability to effectively plan and implement appropriate solutions
- Whether timely and adequate monitoring tools are available to ensure rapid response to stress events.

While boards should not involve themselves in day-to-day organizational oversight, the COVID-19 pandemic has underscored the importance of the board's role as a trusted sounding board and support to management when navigating norm-shattering events and evolving environments. It is precisely in these challenging times that the deep experience of engaged board members can bring necessary insight and clarity.

Introduction

Today's interconnected global economic system exposes businesses to a broad range of risk factors, with more potential points of failure and less room to absorb delays and disruptions. Operating in an environment of volatility, uncertainty, complexity, and ambiguity is likely the new status quo. In an earlier paper, we spoke to the opportunity and imperative for operational resilience brought forward by COVID-19, particularly related to the fundamental, end-to-end supply chain disruption caused by the crisis. Until recently, supply competitiveness was a matter of maximized efficiency / asset utilization and minimized cost / inventory – after all, back-up measures cost money. Yet, efficiency limits flexibility and margin of error. This works well in a low-risk environment, but as we have seen, an acute focus on efficiency does not bode well when supply becomes constrained as a result of uncontrollable external events.

While there are other significant challenges inherent in today's global supply chain model which must be addressed – such as the use of child labour, fraud, bribery, corruption and environmental impacts – this paper speaks specifically to the board's role in navigating the paradigm shift underway – from hyper-streamlined, rigid supply chain models to flexible logistics for a dynamic, demand-driven world. Strategic focus is shifting from cost reduction alone to *risk-adjusted* efficiency and agility, as companies recognize that the new competitive advantage is the flexibility to respond to any array of critical unknowns while continuing to add value and support long-term growth.

The enclosed questions address strategic aspects for boards to consider in their broader oversight activities as well as specific, thematic questions aimed to satisfy the board that appropriately robust supply chain security and agility measures are in place and under control at the management level. Questions are organized under four foundations:



Understanding the Current Situation



Scenario Planning



Implementation



Measuring and Monitoring Supply Chain Risks

Understanding the Current Situation

Questions for directors to ask:

Are there strategies in place with respect to supply chain resiliency?

What will the board's role be in assessing / re-defining supply chain strategies?

What are the key trends and issues affecting the company's supply chains? (e.g., sustainability, labour conditions, etc.)

Directors should monitor that company leaders do not operate or make short terms decisions outside the character of the organization that could affect the long-term reputation, operations or culture of the organization.

What information do we need to meaningfully understand and monitor the company's critical supply chains?

With what frequency do we want to receive this information?

Conducting Situation Analysis

It may be necessary to conduct a data-driven situation analysis to understand the impact of an event on the company's supply chains. When performing the analysis, it is important to look at an array of factors: products and services; competitors; distribution and market channels; environmental, sociological or governance factors; opportunity and issue analysis. The board can play a significant and valuable role in helping management identify blind spots in that analysis, or they may engage a third party for an independent assessment that challenges their assumptions or those of management.

[Appendix 1](#) includes questions that management may consider in conducting a situation analysis.

Scenario Planning

Every decision or plan embodies a degree of uncertainty. While we all agree that decision-making should be based more on facts than intuition, data may be difficult to gather, and more importantly, is historical. Resilient companies must approach their future supply chain strategies with an eye toward the competitive criteria of tomorrow, not historical information.

Scenario analysis is a valuable practice to think critically about whether supply chain interruptions are temporary or indicative of longer-term risks and opportunities. It may also assist in understanding key sensitivities and allow for development of preemptive responses to uncertainties. Scenario planning is not a rigid science. It is a subjective technique to facilitate strategic dialogue and build consensus.

The steps in a supply-based scenario planning process are as follows:

1. Identify the organization's major driving forces and key assumptions pertaining to supply management, including its role as a supplier to clients. Forces may include: supply network, product design, demand shifts, financial position, liquidity, or organizational readiness.
2. Identify certain and uncertain change events likely to have material impact on the business – this could be a market contraction, loss of supply, difficulties in distribution or additional regulatory burden.
3. Develop a range of descriptive, plausible risk- and opportunity-based scenarios surrounding those material change factors, such as: the market contracting by 30%, the company losing two key suppliers, or a competitor exiting the market.
4. Analyze and address the implications of the selected scenarios in the context of the driving forces and assumptions identified in Step 1 and develop action plans surrounding each – whether that is to pursue opportunity or build in operational “insurance” against potential vulnerabilities

Questions for directors to ask:

What scenario analyses have been completed?

What are the key implications and how are they being addressed?

Has management considered the perspectives of critical internal and external stakeholders in identifying current and future opportunities and risks, and its responses?

Implementation

Proactive implementation is what separates resilience planning from strategic planning. Resilience requires flexibility in all aspects of the delivery model – from transportation modes to digitization, sourcing, and product development. Even the best laid plans come down to how well they are translated into action. Especially in times of uncertainty or flux, companies can fall victim to common implementation pitfalls, such as:

- Lack of ownership
- Lack of communication to employees and partners
- Too many or too ambitious goals
- A “tick box” plan developed only because it is expected; lack of employee buy-in
- No plans for implementation, monitoring or revision

Questions for directors to ask:

How will the board regularly monitor the implementation of the company's strategies related to supply chain resilience? Will the full board or a committee of the board be tasked with these monitoring activities?

Are we confident that the organization and its leadership have the desire, skills and confidence to make necessary changes?

Measuring and Monitoring Supply Chain Risks

No matter how carefully a project is planned, monitoring results against expectation is critical in enabling course correction to improve performance and manage risk. It is best to start by asking three simple questions:

1. How are we doing?
2. How do we know?
3. Where must we improve?

Questions for directors to ask:

Is there an appropriate breadth and depth in the key supply chain sensitivities that are being monitored?

If too few sensitivities are monitored, key learnings can be overlooked; too many wastes time and detracts focus. The challenge is to establish just the right balance – carefully monitoring and quickly addressing issues when they arise.

Conclusion

Today's constantly changing geopolitical and environmental landscape virtually ensures that there is always another challenge just over the horizon. Operating in an atmosphere of volatility, uncertainty, complexity, and ambiguity is our new normal. Organizations must understand how their internal and external environments will impact supply chains if they are to respond with agility.

Resilient companies are rapidly preparing to embrace uncertainty, pivoting toward opportunity, and innovating with a long-term view. While these are challenging steps to take – especially in a stressed environment – companies can leverage the resources at their disposal, including an engaged board, to build the necessary structures and capabilities to embrace, and thrive in, uncertain times.

Appendix 1

Suggestions for management in conducting its situational analysis:

Questions for management to consider:

What information do we need to understand the actual circumstances facing the organization today, as well as longer-term strategic impacts on the organization, its supply chain, and the marketplace in which it operates?

What supply chain issues did any recent “black swan” events uncover? How likely is it that other disruptions might cause impacts of a similar nature?

How can we gain comfort that the company’s logistics, operational assumptions, and inventory strategies continue to be relevant in an ever-changing environment?

What effort has the organization taken to determine the parallel resilience of its key suppliers?

Can the organization confidently demonstrate to clients that steps have been taken to guarantee supply in the face of major adversity?

How often do we want to reassess scenarios and our responses?

Pitfalls to avoid while developing scenarios:

- Becoming paralyzed by a multitude of possibilities; keep it simple and focus on two to start.
- Choosing a scenario to plan around; scenario analysis is about exploring all possible outcomes and preparing to address whichever situation arises.
- Focusing too short-term; it is important to look well ahead because organizational change and disruptive events will have secondary and tertiary impacts far into the future.

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