

Business Impact of Coronavirus: Emergence



Report prepared by:

Tim Cummins, President, IACCM

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Tests of public opinion show that people do not want the world to return to the way it was before, a view that is overwhelmingly endorsed by the contracts and commercial community. 88% hope for increased levels of collaboration and a more 'fair and reasonable' approach to negotiations.

As country lock-downs are slowly eased, interest is shifting rapidly to the question of what emergence will look like. This fourth report on the Business Impact of Coronavirus focuses on early indicators of how commercial relationships may change. The pandemic has shown corporate behavior at its best and worst, with some demonstrating high ethical standards of care not only for employees and the local community, but also the impact their actions have on far-flung communities in the poorest parts of the world. Others have simply shrugged off their responsibilities, ignoring contractual and moral obligations, with no apparent care for the consequences.¹

So will things really change? In that same poll where 88% voiced their hopes for new ways, 74% actually believe that they will happen. The infographic below indicates what form those changes may take.

Commerce re-imagined: the time is now



COLLABORATION TO
MANAGE
UNCERTAINTY



A SHARED APPROACH
TO MANAGING RISK



TRANSPARENCY IN
SUPPLY CHAINS AND
ECOSYSTEMS



SIMPLIFYING AND
DIGITIZING FOR A
VIRTUAL WORKPLACE



ESTABLISHING A NEW
BALANCE IN VALUE
ASSESSMENT

¹ See, for example, CNN Business, April 22nd 'Bangladeshi garment workers face ruin as global brands ditch clothing contracts'

Is the situation improving?

Since our last report on April 22nd, the overall percentage reporting a moderate to severe impact from the coronavirus pandemic has fallen from 79 to 75. While this appears insignificant, of greater interest is the fact that those reporting a severe impact has dropped by 7%, from 36% to 29%. A further encouraging factor is that the effect on contract performance has moved up-stream, with a higher proportion now indicating impact on customer contracts and a lower number experiencing issues with their supplier contracts. This implies that supply issues are now flowing through and that the easing of restrictions in some countries, together with the actions taken to identify alternative supply sources, are having positive effect.

Regional variations remain and the largest positive change in this survey has occurred in Europe, where moderate / severe impact has fallen from 73% to 65%.

So where next?

While there remains a considerable need for short-term measures such as finding supply alternatives, it is notable that attention for many is shifting towards the future. As the table below indicates, there has been a substantial increase in the proportion re-evaluating overall sourcing strategies and reviewing both current and future approaches to contract terms.

RE-EVALUATION	% UNDERTAKING	CHANGE IN LAST 30 DAYS
Ts&Cs in current or future contracts	72	+8
Exposure or concentration in particular markets	44	+8
Overall sourcing strategies and market exposures	71	+15
ACTIONS BEING CONSIDERED		
Near-shoring/increasing domestic sources of supply	63	+9
Bringing activities back in-house	49	+11
Reducing exposure in low-cost or emerging markets	40	+9
OBJECTIVE BEHIND ACTION		
Diversify/add to sources of supply	47	+6
Find short-term supply alternatives/additions	37	(5)
Replace existing suppliers	9	(1)

Commerce re-imagined

The series of surveys undertaken by IACCM is pointing towards a number of key areas and initiatives which collectively suggest the new commercial framework that could emerge.

Collaboration to manage uncertainty

Commercial teams appreciate that supply relationships face a prolonged period of uncertainty, with the overhanging threat that coronavirus will recur at unpredictable times and in unpredictable places. The pandemic has confirmed the fragility of many supply chains, undermined by years of aggressive sourcing strategies focused on overall cost reduction.

Moving forward, relationships need to be more adaptive and this requires increased levels of cooperation and trust. These depend on a shift in focus for contract negotiations. Examples of the key areas for discussion include:

- Force Majeure clause. Does it deal with recurring events? Will frustration / impossibility be an option? Does it result in cancellation, or delay?
- What are the termination rights and consequences?
- Payments due or already made for services/goods that become impossible to deliver or unwanted. Can you reach an amicable agreement on this that works for both parties?
- Requests for reduction in volume of products or services, or shift in mix.
- Claiming delay/extending the time for performance. Should there be a time limit? Is there an impact on price?
- Governance terms - consider the elements of relational contracting, such as formal communication protocol, escalation procedures, performance review cycle, innovation incentives.
- Each party should be under notice obligations to notify promptly of any material changes in circumstance. Consider consequences for failure to notify in good time.

A shared approach to managing risk

As the terms above imply, there is a need for far more open discussion about risk and how it will be managed. The pandemic will inevitably leave many corporate balance sheets seriously weakened, reducing the ability to carry risk. Beyond this, the availability of suppliers will reduce, on some estimates by up to 40%. With reduced competition, buyers will find increasing difficulty in switching supply and therefore their leverage will reduce. Collaborative relationships imply a more balanced approach to the traditional risk allocation terms (limits of liability, indemnities, liquidated damages etc.) and greater focus on provisions and practices which assist in the identification and management of risk.

With high levels of market uncertainty, it will be in the interests of both parties to ensure increased visibility that enables a more proactive approach to risk. This will include not only the sort of relational terms mentioned above, but also consideration of improved data flows (e.g. through shared technology platforms) and mutual risk registers. Already, there are indications that one impact of social distancing is more regular and informal 'touch-points' between customers and suppliers.

Transparency in supply chains and ecosystems

IACCM research published earlier this year indicated that there are limited levels of supply chain visibility in most industries and the pandemic not only confirmed this finding, but also revealed its consequences. Many organizations were unable to anticipate or prepare for supply issues because they simply did not know the source of critical components and sub-assemblies.

Gaining increased transparency is therefore a pressing issue, but it is not easy to achieve, not least due to a lack of overall trust within supply chains. Many suppliers fear the motivation of their customer and this will only be addressed through the collaboration indicated above. However, there is also a question over whether supply chains are the way forward. An in-depth IACCM study² found that organizations will increasingly segment supply models through a mix of traditional supply chains, supply networks and supply eco-systems, each of which requires a differentiated model for contracting and relationship management.

Simplifying and digitizing for a virtual workplace

The new environment of increased working from home places added urgency on the ease and quality of communication to support operational accuracy and efficiency. Simplification of process and documentation are pre-requisites to digitization.

Critical business goals depend upon robust data flows. The pandemic revealed the weaknesses of current technologies³. Within Procurement, investment has focused on systems that support standardization and cost reduction. Within Sales, there has typically been little investment in automating the contracting process. There is now wide recognition of the need for appropriate technology but, to make the investment worthwhile, organizations must take steps to simplify:

- Improving definition of existing process
- Standardizing process across the business
- Review or develop improved contract templates, including simplification and design standards
- Develop a clause library with defined fallbacks

Establishing a new balance in value assessment

Sustainability and social value have been growing as issues for several years, but with a very mixed response. Many believe that the coronavirus pandemic will be the catalyst that results in more rapid change. Already, the environmental benefits from reduced travel are becoming evident, but much deeper questions are being asked around aspects of social equality and inclusion. Many governments are developing programs around social and economic recovery and their ability to influence the business agenda will inevitably increase as a result of the debt generated during the pandemic. While there will inevitably be inconsistencies in approach, demands for more balanced assessments of value seem inevitable. It is also clear that, with financial performance inevitably impaired, corporations have the opportunity to make a break from the measurements of the past and to incorporate a new value framework within their contracts.⁴

² IACCM Supply Ecosystem report, April 2020

³ IACCM report 'Managing Contracts Under Covid-19', April 2020 <https://www.iaccm.com/resources/?id=11079>

⁴ IACCM is leading an international working group gathering and disseminating policies and case studies related to social value contracting. It covers both public and private sector initiatives. For more information, contact info@iaccm.com.

Conclusion: Social Disruption or Interruption?

Wikipedia describes social disruption as ‘a term used in sociology to describe the alteration, dysfunction or breakdown of social life, often in a community setting’. Social disruption, it goes on to say, implies a radical transformation in which the old certainties of established society are falling away and ‘something quite new is emerging’.

It is this point about ‘something quite new’ that is of particular relevance. Will the coronavirus pandemic result in ‘radical transformation’? Seemingly disruptive events do not necessarily lead to significant change. The Global Financial Crisis was assumed by many to represent an inevitable turning point, when society would turn against the system that had allowed such a catastrophic event. Yet it did not. By and large, that old system re-asserted itself,⁵ although arguably it contributed to growing levels of democratic disconnection, polarization and fragmentation which have manifested themselves in geopolitical volatility, such as the rise of populism.

In an excellent article⁶, The Guardian newspaper highlights how negative or unexpected consequences might well happen again, as a result of the pandemic. For all the delight about falling levels of pollution and the potential this offers to advance the environmental agenda, it reports the loosening of environmental controls in both the US and China. Authorities there have used the economic effects of the pandemic as an excuse to roll back regulation – suggesting that the ‘disruption’ we experience could in fact be in the very opposite direction of what we hope for. Similarly, the pandemic has introduced far greater and more intrusive social controls, including greater use of spy cameras, drones and the use of the security forces to oversee social activity. Will they become ‘the new normal’?

How and in what ways these reactions manifest themselves depends a lot on the nature and scale of the disruption and the ability of the affected community to act. In a recent article, Harvard Business Review tackled the question of why today’s best funded and most expensive health and education systems frequently under-deliver to the societies they serve. It concluded that ‘Organizations are wedded to their current solutions, delivery models and recipients’, meaning that investment is focused on maintaining the status-quo, standing in the way of simplification and innovation. This results in the delivery of ‘good enough’, rather than excellent, services.

Whether the hopes and aspirations of the contracts and commercial community will be realized is therefore far from certain, though the forces outlined in this report make it highly likely. It is also important to recognize that the community itself has influence and can collectively promote these values of increased collaboration and balance, of a broader assessment of value.

⁵ ‘Never let a serious crisis go to waste’: Philip Mirowski, published by Verso, 2013

⁶ ‘We can’t go back to normal: how will coronavirus change the world?’ The Guardian, March 31st 2020



About IACCM

IACCM is a not for profit association active in over 170 countries, with a mission to improve the quality and integrity of trading relationships. With more than 60,000 members representing over 17,000 organizations, IACCM is dedicated to raising individual, organizational and institutional capabilities in contracting and commercial management. It achieves this by providing research, benchmarking, learning, certification and advisory services to a worldwide, cross-industry audience of practitioners, executives and government.

For more information,
please contact:

Research@iaccm.com

www.iaccm.com

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