SUPPLY CHAIN FUNDAMENTALS

Supply chain management is key to the success of every retail business. Today's consumers expect good value, continuous availability and products which are produced with respect for the environment and human rights. In recent months, a number of high profile stories have hit the headlines, highlighting the difficult line that businesses must tread in managing their supply chains.

Know your supplier

Adopt robust procurement processes to identify key legal and reputational risks. For example, does a potential supplier present a clean bill of health on areas such as bribery and corruption risk, and tax compliance risk? To what extent does it rely on slave labour or raw materials which have been produced using slave labour? Increasingly, failures by your suppliers in these areas can get you into trouble. In the UK, anti-slavery laws require large businesses to report on what they are doing to identify and prevent slavery and trafficking in their supply chains. Anti-bribery and anti-tax evasion laws provide that criminal offences can potentially be committed by businesses as a result of the activities of certain trading partners.

Pay particular attention to those suppliers on whom you rely the most. Have they convinced you of their ability to perform their side of the deal? For those businesses, especially those who you have identified as being at high risk of failure, consider undertaking an end-to-end supply chain review. This will help to highlight potential weaknesses so you can plan for these. Consider the counterparty's reputation and credit worthiness and who has the balance of power in your trading relationship with them. Where possible, strike a balance between getting a good deal and becoming over-reliant on any particular supplier.

Know the market

Smart use of market intelligence can help protect you against weaknesses and risks in your supply chain. Consider where this knowledge sits in your own business, and which third parties can help you stay close to supply markets. Think laterally – give thought to how factors such as global political events and trends in public opinion could affect supply and demand. What will be the knock-on effect for your suppliers? Can they cope? How quickly could you switch to a new source of supply without compromising quality or your onward supply commitments?

Ensure you are having regular conversations with those who can keep you informed. Also, review sources of qualitative data, such as the press and campaigners. These can help you spot markets and territories which are vulnerable to the kind of risks identified above.

Take time to agree detailed terms before supply commences

Agreeing the commercial deal is only part of the story. It is also key to ensure that each party understands clearly what is expected from it and that you have rights that you can exercise if it starts to look like the relationship is not going to plan. In particular, focus on:

- what standards the supplier must meet, and what rights you have if those standards are not met
- payment terms and your ability to set off sums due to you
- your ability to terminate and consequences of termination
- retention of title or securing collateral for contractual obligations
- ownership of key data
- ensuring that the agreement is clear on timing and quantum of price changes, and on whether forecast volumes are binding (or when they become binding)

For longer term agreements, consider what "future proofing" may be required. For example, for agreements which will continue post-Brexit, it would be wise to pay particular attention to price change mechanisms and force majeure provisions.

Watch out for insolvency red flags and know how to act on them

The sooner you can identify insolvency red flags in your supply chain, the more you can do about them. Potential insolvency red flags include:

- Macro-economic changes, for example changes in supply / demand
- Regulatory change
- Decline in reputation
- Declining profit/KPI's
- Failing service levels
- Re-launches and rebranding
- Avoiding communication
- Staff turnover, redundancies
- Concerns around trade credit insurance

If you identify any of these, engage early with affected suppliers to understand more. At this stage, you can carry out an analysis of your potential options. Where the impact of failure is high, consider carrying out a business plan review of suppliers and customers to ensure due diligence has been taken to review their supply chains and identify any risks that may flow through to your business.

Have a plan B

It is important to have a backup plan to prevent major losses if a key supplier fails to perform. Recently, KFC hit the headlines when failure of its logistics supplier led to a shortage of a key ingredient: chicken. It transpired that KFC had recently switched logistics suppliers in a move which reportedly prioritised cost savings over quality of service. In all, it seems to have been a costly decision, as the restaurant chain was forced to temporarily close two thirds of its branches. Similarly, when grocery and tobacco wholesaler Palmer & Harvey went into administration late last year, supermarkets were required to deploy contingency plans to ensure they could continue to meet customer demand.

Appointing a supplier on an exclusive basis has both benefits and risks. Clearly, the advantages of being able to negotiate a better deal and the convenience of managing just one supplier are significant. However, the consequences of supplier failure can be great, as the experience of KFC shows. Thought should also be given to creating a seamless lead-in and lead-out when changing suppliers. There is a risk that a dissatisfied outgoing supplier may fail maintain service standards. Careful handling of the changeover may be required to avoid interruptions in supply and to deal with stock effectively.

Our specialist Retail & Consumer lawyers can advise on all aspects of the supply chain lifecycle. Please contact us to discuss how we can help you solve the specific issues concerning your business.

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