COVID-19 impact assessment: Mitigating against supply chain disruption in Africa

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With the rise of globalisation over the past three decades, the world has become increasingly interconnected, not least in the production of goods. Between the extraction of natural resources and final sale of products to the consumer, raw materials and intermediate goods can be shipped around the world multiple times, and processed in numerous jurisdictions. The impact of COVID-19 on these global supply chains has been severe – a twin supply-demand shock where production and consumer appetite have been simultaneously eroded.

Africa, like other regions worldwide, faces significant supply chain disruption resulting in unprecedented challenges. Despite the undoubted severity of the current crisis, there remain steps that businesses should take in the short-term to manage the impact of COVID-19 on their supply chains. The pandemic also provides a stimulus for a fundamental strategic re-evaluation of how executives manage their global supply chains, where Africa moves from primarily being a provider of natural resources, to also being a production site serving both fast-growing domestic markets, and international consumers. If investors can overcome the current disruption, their focus should turn to the long-term. Reformulating the role that Africa plays in global supply chains can help businesses bolster resilience, mitigating against future operational risks.

The current situation: Severe disruption throughout Africa's supply chains

Across various sectors, notably mining, oil and gas, manufacturing and agriculture, Africa forms an integral part of global supply chains. At every stage of these, businesses have been beset by challenges, compounding the considerable operational complexities that already exist within many countries on the continent.

By providing raw materials, Africa constitutes the anchor of many international supply chains. Resources ranging from oil to coltan represent essential inputs for goods including clothes and mobile phones. Yet, throughout the continent, COVID-19 has led to a widescale and abrupt halt in production. In South Africa, on 23 March, global mining companies such as Rio Tinto were forced to suspend their operations after the government ordered the closure of all mines, exempting only those supplying coal to state power utility Eskom. As of 16 April, mining resumed, but at a reduced operational capacity of 50 percent, prolonging the damaging impact of COVID-19 on miners' bottom lines. In the Democratic Republic of Congo, Canadian mining company Ivanhoe's decision to suspend operations at its Kipushi copper mine has influenced a group wide cost-cutting spree, with the business recently announcing targeted savings of USD 75 million through 2020/21.

For oil companies operating in Africa, the financial impact of COVID-19 has also been significant. Production has slowed as global demand for petroleum has faltered. In China, the largest market for African oil, COVID-19 induced factory closures resulted in manufacturing falling by 13.5 percent in January and February, compared with the same months in 2019, according to the World Economic Forum. In response to this fall in demand, IOCs across Africa have slashed production and cut budgets, while also pausing new exploration.

While not a major manufacturing base within most global supply chains, Africa has been far from immune to the effects of COVID-19 in this sector. As with other regions globally, Africa has experienced factory and industrial park closures. Last month, German automobile manufacturer Volkswagen shut down its plants in South Africa and Rwanda, as national lockdowns and falling global car sales provided a double-headed supply-demand hit. Africa's commercial relationship with China has further compounded the problem. With the continent's manufacturing sector heavily reliant on Chinese made components, China's industrial slowdown has resulted in a dearth of inputs required for industrial production.

Lacking sufficient domestic manufacturing capacity, supply chain disruption for medical imports to Africa have also presented challenges for governments responding to the pandemic. With the continent behind the infection curve of China, the US, and Europe, much of the global stock of personal protective equipment and COVID-19 tests has already been purchased. Furthermore, many of Africa's conventional sources of medical supplies — notably China — have introduced export restrictions on these goods, compounding their inaccessibility for governments on the continent.

Further along the supply chain, pre-existing logistical challenges in Africa resulting from poor transport infrastructure have been exacerbated by COVID-19. While the decisive action taken by many African governments to swiftly close or increase checks at their borders and ports has been praised for curtailing the spread of the virus, it has added a new obstacle for businesses transporting raw materials and goods. This has been particularly so for the many agriculture companies active on the continent, who have had to contend with delays when moving perishable and refrigerated products. Beyond these immediate challenges, a longer-term impact of COVID-19 on African supply chains is a delay in the implementation of the African Free Trade Continental Area. The landmark agreement – intended to boost pancontinental trade and interconnectivity – is now supposed to commence in January 2021, delayed from a planned start date of 1 July 2020.

Managing the fallout: Short-term actions companies should take

The severe impact that COVID-19 is having on every stage of supply chains across Africa is clear. Yet, companies can implement short-term measures to manage, and reduce, the virus' fallout. Below, we outline four key recommendations for businesses to follow.

1. Protect workforce

First and foremost, companies should protect the health of their workers. While Africa has thus far experienced comparatively low infection and death rates – though acknowledging that testing on the continent has been relatively limited – caution should still be exercised. The weak healthcare capacity of many African countries means that the potential impact of COVID-19 remains severe.

Companies should adopt workplace safety guidelines, as outlined by multilateral institutions such as the World Health Organisation, as well as the respective governments of the countries in which they operate. Measures are likely to include educating employees on COVID-19 symptoms and prevention methods such as hand sanitisation, thorough workplace cleaning, and implementing social distancing, where possible. From a business ethics standpoint, such action is the right course to follow. However, comprehensive workforce protection also offers commercial advantages. Those companies with robust safety measures are best placed to maintain their place in existing supply lines, and will be able to adapt to the 'new normal' in the coming months.

2. Transparent supplier and customer engagement

As across the globe, businesses in Africa should take steps to understand the constraints of both their suppliers and customers by engaging in open dialogue. Gaining visibility on a supplier's ability to deliver on pre-existing or new orders will help companies to ensure business continuity by altering production, or rerouting supply chains, as necessary. As part of this, companies should ask how they will be treated from an allocation perspective in the event of capacity and inventory shortages. Conducting demands assessments is equally important. Understanding alterations in customers' requirements is essential in mitigating against over production. This is particularly true for African businesses operating in the agricultural sector, where a build-up of perishable stock can result in significant financial losses.

3. Engage policymakers

The dynamic nature of the COVID-19 pandemic has, to a large degree, forced governments to formulate policy 'on the go'. Despite this, companies should still engage governments. Gaining sight of likely future policy changes will help businesses conduct forward planning, for example, ordering manufacturing inputs in anticipation of rising customer demand following a lockdown ending, or preparing goods for transportation as ports are readied for reopening. In some African jurisdictions, communication with governments through formal channels can be difficult at the best of times – in the current environment, even more so. Businesspeople should draw on personal relationships with policy makers, activating their informal networks to gain information. Utilising trusted third parties to receive real time intelligence can also be an effective way of understanding likely policy developments.

4. Support government

Interactions with government should also be focused on offering support to tackle COVID-19. In addition to representing good corporate social responsibility, doing so will help companies to build long-term amicable relationships. In Africa, several multinationals have rerouted their supply chains to bolster healthcare capacity. Diageo's Kenyan subsidiary, East African Breweries, for example, has begun providing grain neutral spirit – an ethyl alcohol used in the production of vodka and gin – to hand sanitiser manufacturers. With many African governments facing shortages in medical and personal protective equipment, helping to provide them represents a worthwhile public relations initiative, while also bolstering critical supplies.

Building resilience: Reassessing Africa's position in global supply chains

Moving beyond short-term risk mitigation, companies should fundamentally re-evaluate their global supply chains, and the role that Africa plays within them. The COVID-19 pandemic has dramatically exposed the vulnerability of established operations. For decades, low costs and minimal inventory have been the guiding principles of supply chain management. With its cheap labour and well-developed industrial infrastructure, this focus has resulted in China becoming the world's factory. Consequently, given the number of companies that source or manufacture products there, the impact of COVID-19 on global supply chains has been momentous. As China went into economic lockdown, businesses across the world suddenly lacked vital inputs, forcing them to close assembly and processing operations.

Looking ahead, companies will seek to mitigate against the supply chain shocks currently being experienced due to over reliance on China. As Larry Fink, CEO of global asset manager BlackRock, recently told *The Financial Times*, "there's going to be a review of supply chains at every company in the world." Moreover, while a health pandemic like COVID-19 has not been experienced in living memory, major economic disruptions look set to continue. Geopolitical turmoil and climate-related disasters have become the norm in recent years, and this trend shows no sign of abating, which will cause further complications to building supply chain resilience. The US-China trade war, for instance, battered the operations and profits of foreign companies – particularly manufacturers – based in China, with many businesses relocating in order to avoid damaging tariffs. The COVID-19 disruption currently being experienced is not an isolated incident, and going forward, risk mitigation, as opposed to just cost management, should influence supply chain strategy.

The need to diversify global supply chains away from China is clear. Given, however, the predominance of China in manufacturing, component sourcing and product assembling, a wholesale move to new jurisdictions in the short and medium-term is unfeasible. Shifting sites of production will necessarily be limited and gradual. This said, already there are a number of well-established non-China manufacturing centres. In recent years, for example, Nike, Adidas and Samsung have all began shifting production to Vietnam; countries including Brazil, India and Thailand are also becoming increasingly important manufacturing bases in global supply chains.

When considering diversification options, however, corporations should include Africa in their considerations. Various countries on the continent offer many of the benefits provided by China and other more well-established alternatives. Africa's population of 1.2 billion, with a median age of 19.7 years, represents a substantial, youthful workforce. There are few jurisdictions in the world that can match the size and affordability of labour in investor-friendly African countries.

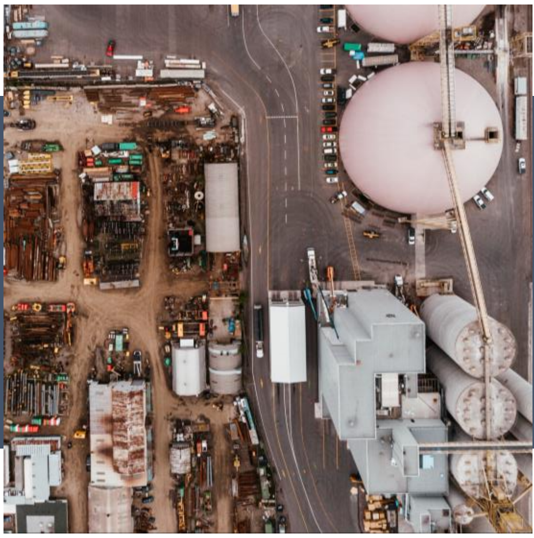
Moreover, like those of many South American and Asian countries, numerous African governments have made industrialisation a key objective, and offer attractive incentives to investors establishing operations in their countries. Ethiopia, for example, which aims to be the leading manufacturing hub in Africa by 2025, provides custom duties and income tax exemptions in this sector. Such incentives led PVH Corp., one of the largest apparel companies in the world, to establish a manufacturing base there in 2017. Morocco, likewise, has made the establishment of free trade zones a key part of its plan to attract foreign manufacturers, with companies operating within them exempt from paying corporate income tax on their profits for five years. The Kingdom’s strategy is working, securing the arrivals of multinationals including car and plane manufacturers Renault and Bombardier in recent years.

Beyond providing many of the benefits apparent in China and other jurisdictions, diversifying supply chains to Africa affords advantages in its own right. With the continent providing many of the raw materials that are essential manufacturing inputs, locating production sites in Africa could shorten supply chains, thereby reducing logistical risks and costs. Similarly, many jurisdictions in Africa offer geographic proximity to key consumer bases compared with China and other Asian countries – North Africa to Europe; East Africa, the Middle East; and West Africa, the US. As companies look to boost supply chain resilience, reducing the distance between manufacturing bases and markets is imperative. Multinational Inditex, owner of clothes brand Zara, already has major production sites in Morocco, a short distance from its number one market – Spain.

With the UN forecasting that Africa’s population will hit 2.5 billion by 2050, another advantage that the continent offers manufacturers is a growing, and increasingly prosperous, domestic market. Locating sites of production within potentially lucrative markets has obvious supply chain benefits, enabling companies to cut down on transportation time and costs, and boost resilience. As Coca Cola CEO James Quincey recently commented when reflecting on the impact of COVID-19, “a great strength has been the local production of Coke’s soft juices and drinks... The drinks in Kenya are made in Kenya”. As Africa’s markets grow, this supply chain resilience will only increase in importance.

Emerging from the crisis: Coming out stronger

In Africa, as across the world, supply chain disruption looks set to continue for the remainder of 2020 and, quite possibly, beyond. For companies operating in already complex African jurisdictions, the challenges faced are unprecedented. However, the COVID-19 pandemic provides stimulus to build resilience; implementing short-term risk mitigation measures and reformulating supply chain strategies will only strengthen companies’ ability to respond to future operational threats. As businesses navigate COVID-19, grasping this opportunity is key.



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