



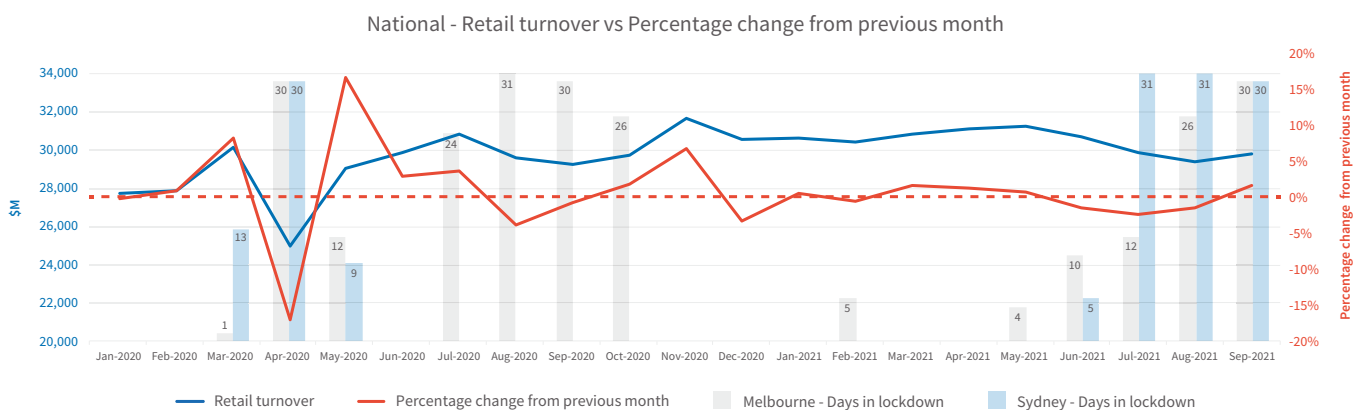
ARTICLE

# Supply chains and volatile demand: how to navigate these challenges

The retail sector has always been competitive and business survival requires both acumen and luck. Retailers quickly feel the brunt of unanticipated changes in business conditions. Retail trade data released by the Australian Bureau of Statistics shows how much harder business has become for retailers since the pandemic. This article explores volatility in the retail sector, supply chain constraints, and some considerations for retailers to navigate these challenges.

Although the retail sector has continued to grow throughout the pandemic (from \$27.8 billion per month in early 2020 to over \$31 billion in October 2021), the increase in volatility of demand is striking (refer to Chart 1). Prior to the pandemic, retail turnover volatility varied from -0.5% to +0.9% on a month-to-month basis. The initial months of the pandemic in early 2020 saw monthly variability drastically increase from -17.4% to +16.6%. Over the past year, the monthly variability has levelled out yet remained high at -4.1% to +6.7%.<sup>†</sup> These estimates are seasonally adjusted to remove variation that is repeated at regular intervals (such as cycles of seasons or holidays), and as such, the increased variability can be considered out of the norm.

**Chart 1: Monthly percentage change in Australian retail turnover, seasonally adjusted estimates (current prices), and days in lockdown in Sydney and Melbourne**

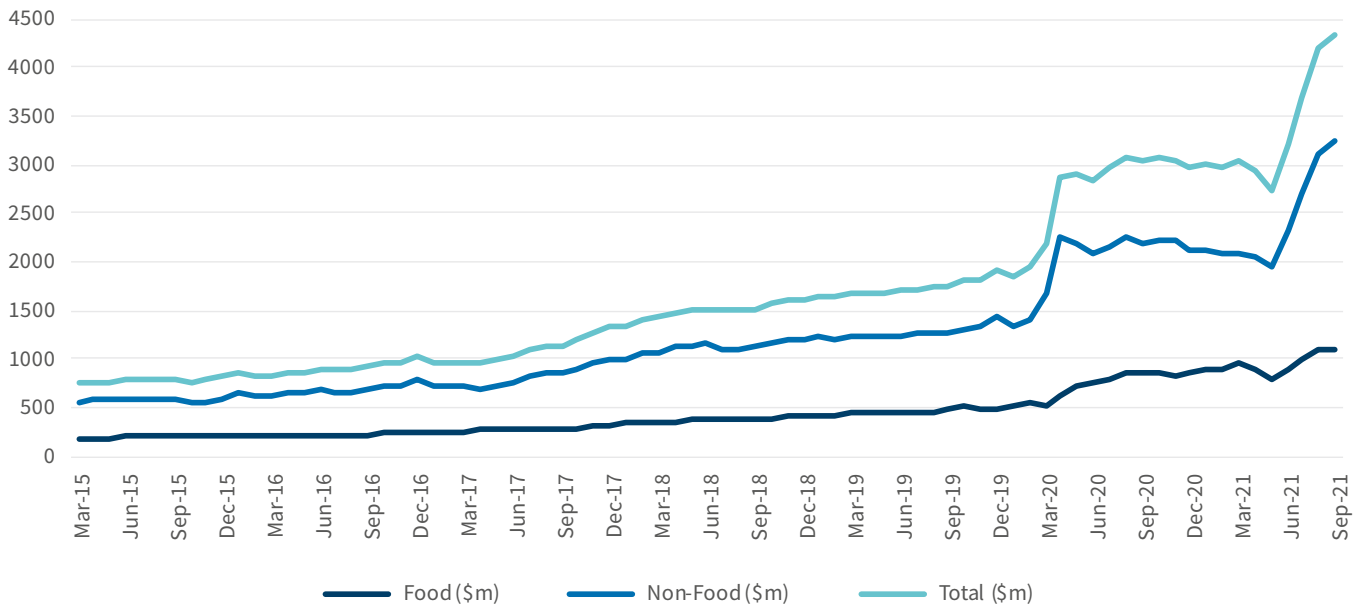


<sup>†</sup> Source: Australian Bureau of Statistics, Retail Trade, Australia September 2021. Source data on lockdown days is based on government press releases and news publications of restrictions.

COVID-19 has accelerated changes in consumers’ preferences for online retailing. Online retailing has grown +100% in both non-food and food categories, and now represents circa 15%<sup>1</sup> of total retail turnover (refer to Chart 2). This increased e-commerce penetration has been largely sustained, despite the re-opening of retail stores,

and many analysts including experts at FTI Consulting are expecting the shift to e-commerce to continue. The relative stabilisation of national retail turnover in recent months also points to the role of this e-commerce transition.

**Chart 2: Online retail turnover, seasonally adjusted, \$ millions**



Source: 8501.0 Retail Trade, Australia: Table 21: Online Retail Turnover, Australia, by type of activity, September 2021.

**MANAGING INCREASED DEMAND VOLATILITY**

Channels to market, customer experience, and stock management are key factors to managing increased demand volatility.

At the firm level, the challenge for retailers is how to meet customer experience requirements and adapt in line with customer values. In many businesses, this can be achieved through optimising online sales platforms and product lines to enhance convenience. Woolworths is doing so through its recently announced new ‘marketplace’, which will double its online product range. Greater online sales also require good logistics contracts to ensure timely shipments direct to the customer.

Such a transition to a greater online retailing presence has been difficult to manage given that just about every part of the supply chain is experiencing disruptions for both domestic and international businesses. From factory shutdowns due to widening energy power shortages in manufacturing regions in China to the diversion of ships away from usual ports to deliver PPE and vaccines, retailers are experiencing delays in product delivery times, skyrocketing freight costs in excess of 300%, and limited product availability.<sup>2</sup> These challenges are expected to stay, with domestic and international freight disruptions expected until at least mid-2022.<sup>3</sup>

<sup>1</sup> It is possible that the value of online purchases has been under-reported since April 2020 (however the total retail sales will not be under-reported) (refer to ABS for guidance).

<sup>2</sup> Powell, D. 2021. ‘Supply chain crunch threatening Christmas to persist until 2023, DHL boss warns.’ Written for The Age, 23 November 2021, accessed online November 2021, at: [https://www.theage.com.au/business/companies/supply-chain-crunch-threatening-christmas-to-persist-until-2023-dhl-boss-warns-20211122-p59axk.html?utm\\_content=TOP\\_STORIES&list\\_name=2033\\_age\\_busnews\\_am&promote\\_channel=edmail&utm\\_campaign=business-am&utm\\_medium=email&utm\\_source=newsletter&utm\\_term=2021-11-23&mbnr=MzA2MTgwMTY&instance=2021-11-23-07-12-AEDT&jobid=29347302](https://www.theage.com.au/business/companies/supply-chain-crunch-threatening-christmas-to-persist-until-2023-dhl-boss-warns-20211122-p59axk.html?utm_content=TOP_STORIES&list_name=2033_age_busnews_am&promote_channel=edmail&utm_campaign=business-am&utm_medium=email&utm_source=newsletter&utm_term=2021-11-23&mbnr=MzA2MTgwMTY&instance=2021-11-23-07-12-AEDT&jobid=29347302)

<sup>3</sup> Ibid.

## SUPPLY CHAIN CONSTRAINTS AND CONSIDERATIONS

Given the supply chain constraints, the balance between ‘just-in-time’ deliveries and ‘buffer stock’ should be reviewed. As a result of supply chain issues, many retailers are holding significantly more inventory – some have 20% to 30% more than pre-COVID-19 levels. This may extend to requiring suppliers along the supply chain to have more inventory not only more finished goods. It can have a significant impact on working capital and funding requirements, yet it is one of the more viable options for many retailers compared to, for instance, using air freight to bypass international shipping.

Another challenge is to manage potentially greater inventories including consideration of minimising stock damage or loss. Retailers must also retain inventory visibility across the supply chain to provide up-to-date stock availability information to consumers.

Space considerations are shaped by the range of modified channels to market and evolving customer preferences such as for less contact. Considerations for retailers may include how many and which locations to retain, as well as how to use space - for traditional foot traffic or to facilitate new safe delivery options or use space as mini distribution centres (for warehouse and dispatch).

Retailers will also need to assess supply-chain risk and their supplier’s strategies for ‘reshoring’ or ‘nearshoring’ and the impact this will have on their unit costs. Another aspect to this supply chain reconsideration will be to address the growing focus on ESG considerations, not least of all Modern Slavery issues. This is a further example of how a change in demand experienced by a retailer transmits to manufacturers and importers.<sup>4</sup>

## DEMAND VOLATILITY HERE TO STAY

Greater demand volatility seems likely to remain a feature of the competitive environment in retailing post-pandemic<sup>5</sup> making future business models in need of not so much a pivot but a fundamental rethink. There are four key aspects to this for retailers:

1. Adapting their inventory management and systems to understand the risks in their supply chain and diversify these risks through identifying alternate sources of supply and potentially through different service lines.
2. Having appropriate funding and working capital, along with effective communication of those requirements with lenders or alternate capital providers.
3. Effectively communicating this story with their customers and broader stakeholders so as to not diminish brand reputation.
4. Building in additional ESG requirements to reflect changes to operations and impacts on ESG considerations that are necessary in responding to the current supply chain pressures, and communicating those attributes to the customer.

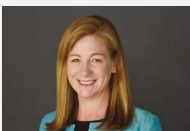
While the current focus is on the challenges faced by retailers in the lead-up to the Christmas season, it is clear the effects of global supply chain constraints will persist well into 2022 and beyond. As the impacts of supply chain and stock constraints persist, retailers will also likely face increasing pressure from a reputation management point of view so it will be important for them to prepare robust plans to communicate to customers, investors, and the media. Attention will initially be on consumers and the effect of stock and supply issues on holiday and celebration planning, placing retailers in the spotlight, but once this has been established as a media narrative, it will only become a larger issue into 2022.

<sup>4</sup> Kardex, 2021. ‘15 Ways COVID is Changing Warehousing and Distribution Forever’. Accessed online, September 2021, at: <https://us.blog.kardex-remstar.com/15-ways-covid-changing-warehousing>.

<sup>5</sup> Productivity Commission, 2020. ‘The COVID-19 Recovery: A view from the supply side’. Speech delivered by Michael Brennan. Accessed online, September 2021, at: <https://www.pc.gov.au/news-media/speeches/covid-recovery>

## HOW WE CAN HELP

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