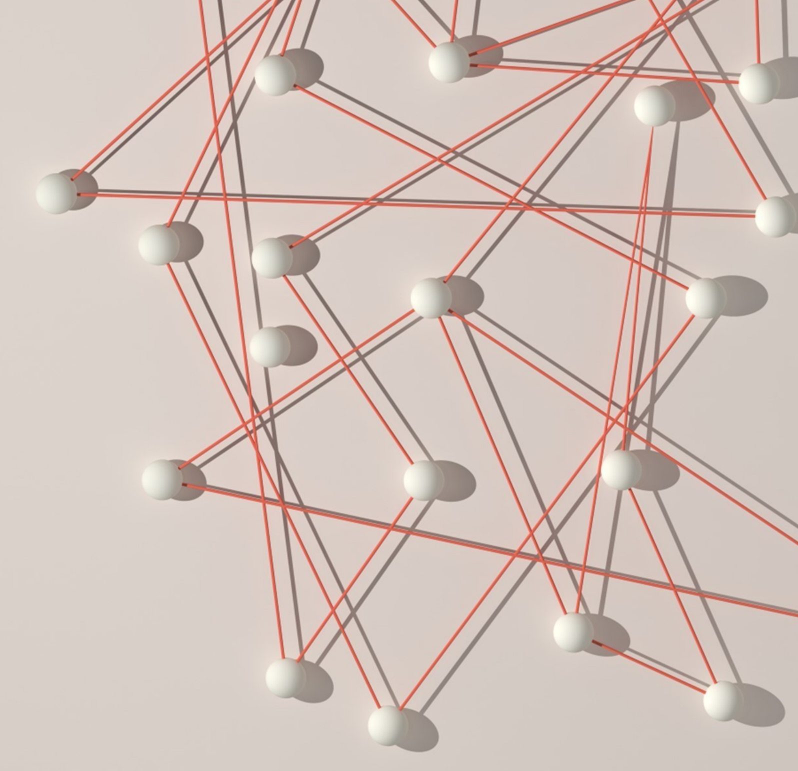
Wilson Perumal & Company



RIGHT-SIZE YOUR GEOGRAPHIC FOOTPRINT

The world continues to see lingering effects from the Covid-19 pandemic. While demand has exceeded pre-pandemic levels in many cases, supply has been unable to keep up. Semiconductor shortages have led Ford to shut down assembly plants and stockpile thousands of chip-less vehicles in lots. In Q1 Ford reported losses of over $3B due in part to these shortages, and experts believe the shortages could last well into 2024. Beyond production shortages, organizations are also contending with port delays, truck driver shortages, and employee turnover.

Globalization has been trending up for decades, but companies are beginning to see downsides to this strategy. Aside from supply chain challenges, overexpansion can introduce additional market, operational, and regulatory risks—as seen by the large number of organizations exiting Russia due to sanctions.

While there are benefits to a global footprint—including potential for lower costs or specialized capabilities—we expect an acceleration of geographic rightsizing and supply chain localization. This is partly a correction to the rampant overseas expansion over the last two decades. The fact is, many companies have passed the point of diminishing returns and are now operating in too many countries.

It's not about the individual country, it's about the portfolio.

For many organizations, a tighter configuration of core countries would be beneficial—and more profitable. Like a company that offers too many product choices, it's possible to make a case for each additional expansion choice, despite the dilutive effect of the aggregate.

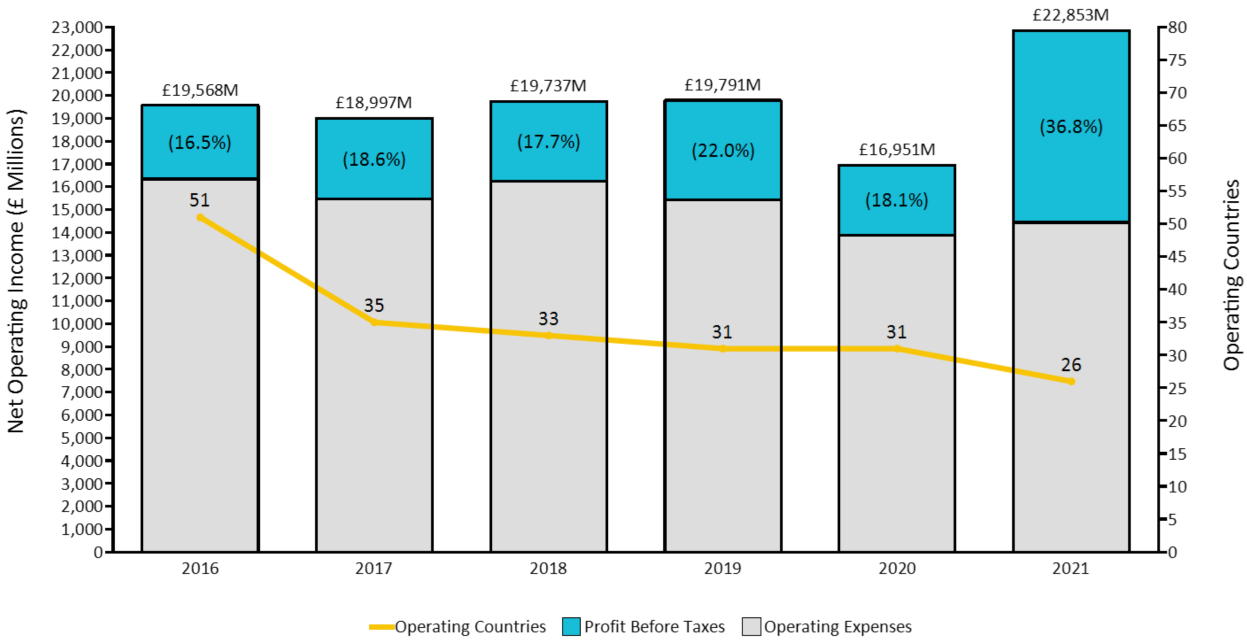
British multinational bank Barclays experienced the effects of overexpansion first hand. Throughout the early 2000s Barclays was rapidly expanding into emerging markets—including expansions across Africa and South America through their takeovers of Absa Group and Lehman Brothers. By 2015, Barclays had subsidiaries and related undertakings in more than 50 countries across the globe.

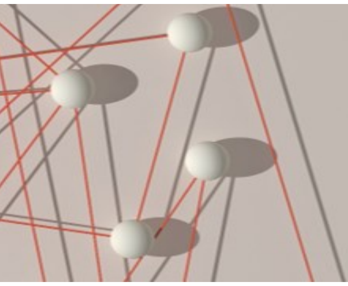
Cracks began to appear in this strategy following the global financial crisis when regulators implemented new rules making it challenging for multinational banks to own large banks abroad. In 2016, Barclays decided to sell their Africa business amid falling profits and an increasingly challenging

FIGURE 1

BARCLAYS FINANCIAL JOURNEY, FROM OVEREXTENDED TO RECOVERY

Barclays operated in over 50 countries in 2016, cutting that number in half by 2021—now operating in approximately 26 countries





Spreading operations across more GMCI groups with widely varying levels of complexity has a direct, negative impact on operating margin. Conversely, retrenching to fewer groups can boost profitability.

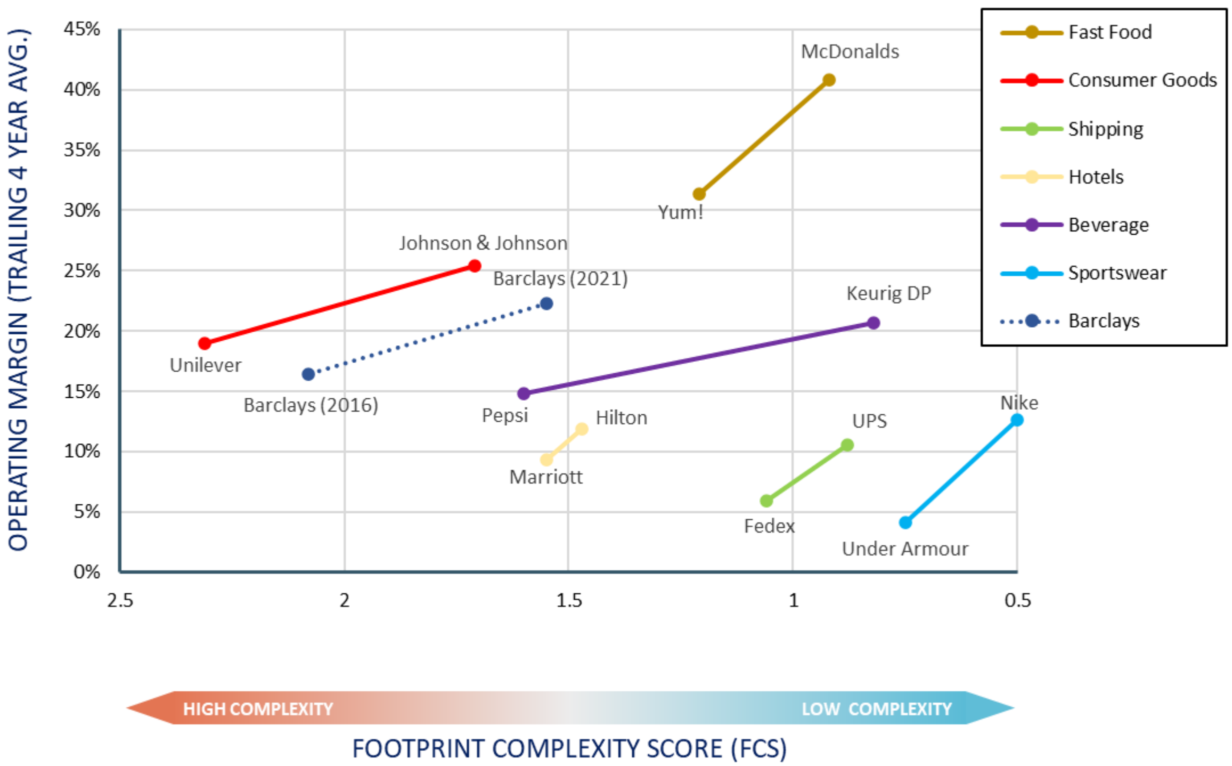
regulatory environment. By 2021, Barclays had decreased their subsidiaries and related undertakings from 51 countries down to 26. Despite stable or decreasing revenues over this time period, Barclays was able to increase profit and margin (from 16.5% in 2016 to 36.8% in 2021).

Other multinationals demonstrate similar results when comparing geographic footprint complexity to profitability. To assess this, we began by calculating a **Footprint Complexity Score** (FCS), a measure of how far afield companies have expanded in terms of the number of **Global Markets Complexity Index** (GMCI) groups in which they operate. An FCS is calculated by summing the percentage of a company's operating countries in each group multiplied by how far that group is from home base.

We then identified close competitors across a range of industries to compare different geographic strategies and how that impacted profits. We focused on "apples to apples" comparisons—Keurig Dr. Pepper and Pepsi; UPS

FIGURE 2

MULTINATIONALS WITH LOWER FOOTPRINT COMPLEXITY ENJOY HIGHER OPERATING MARGINS



and FedEx; Hilton and Marriott, and so on. While there are, of course, many different dynamics at work, we wanted to understand whether there were broad patterns.

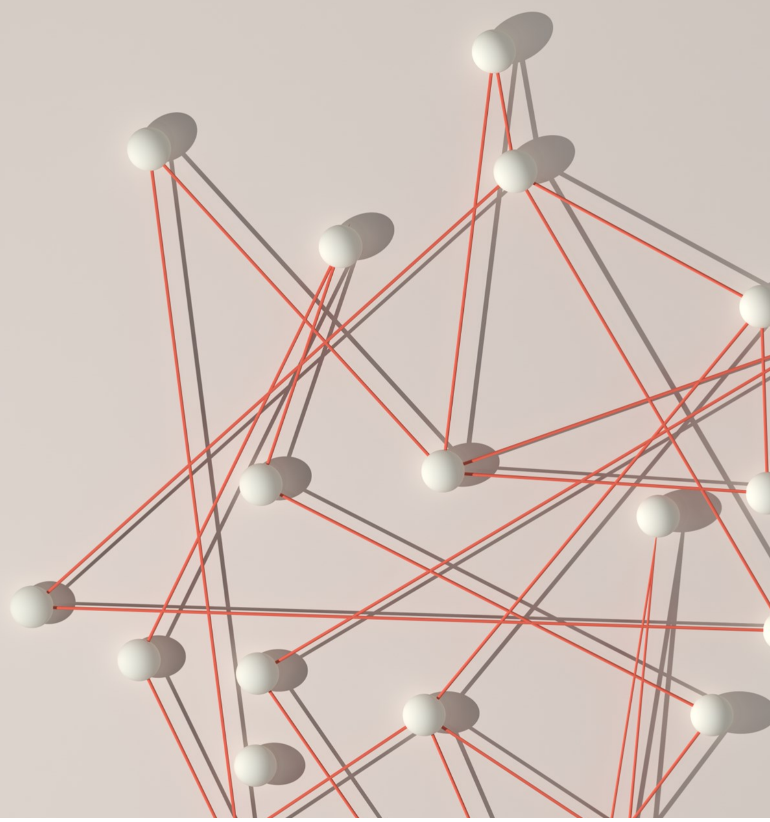
Would two close competitors with different geographic footprint strategies see different levels of profitability? The answer is a resounding 'yes.'

On average, in the examples included here, decreasing the FCS by 0.25 improves your operating margin by 6%. This would be the equivalent of Barclays exiting a country in **Group 6**, or two countries in **Group 4**.

If we accept for a moment that there is a predictive relationship at work, then we would expect to see the company's operating margin improve from 22% to 28%. That is a substantial jump, and while we recognize there are myriad factors driving profitability, the link between FCS and Operating Margin is consistent across a broad set of industries.

Of course, like any top-level metric, we suggest it be used to stir debate, as another point of comparison with competitors, and to build alignment around the issue and the opportunity.

How does your current geographic footprint align with and support your overall strategy?



From a financial perspective, once you consider all of the hidden complexity costs, which markets and regions are truly delivering a return on investment?

Assessing and simplifying your geographic footprint requires a structured approach and robust analysis, but success can unlock significant profitability.

An overview of our approach is below in Figure 3.

LET'S DISCUSS YOUR GEOGRAPHIC FOOTPRINT >

FIGURE 3

WP&C'S APPROACH TO RIGHT-SIZING YOUR GEOGRAPHIC FOOTPRINT

	1 ALIGN ON THE OPPORTUNITY	2 BUILD OUT THE FACT BASE	3 ASSESS ALTERNATIVES	4 PLAN FOR EXECUTION
ACTIVITIES	Conduct GMCI FCS analysis Align on objectives of the project and impact of complexity Clarify role of geographic footprint in overall strategy	Conduct strategic review of the country portfolio Conduct financial review, leveraging Square Root Costing Develop hypotheses for deeper investigation	Assess long list for strategic, financial and operational viability; exit or reduce cost of operations, or refocus resources Refine the business-case Narrow options down to "short list" for further evaluation	Analyze each short list option and finalize the planning for country exits & operating model restructuring Identify cost-out actions enabled by retrenchment, and based on benefit/risk assessment; prioritize options for execution
OUTPUT	Clear objectives and executive alignment Understanding of complexity	Country fact-base including country-level profitability Quantification of complexity costs in the footprint 'Long list' of opportunities and business cases; GMCI outliers, strategic outliers, unprofitable countries	Short list for execution planning Clear business case, including investment requirements Articulation of business risks	Best path for retrenchment based on pressure-testing of plans