Get Your Capital Acquisition Process in Gear

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To compete and win in today's marketplace, manufacturers have begun to re-evaluate what was once a technical undertaking and an administrative afterthought: the capital acquisition process. For decades, multi-million dollar decisions about essential equipment buys have been left to the engineering department, and while their in-depth knowledge is essential, achieving real efficiency and real savings requires something more. It requires multi-site planning. It requires deep market knowledge and global sourcing abilities. Ultimately, it requires a new way of approaching the mission of procurement — one that combines technical excellence with an ability to source material, negotiate strong contracts, pursue energy efficiency incentives and obtain the best total cost of ownership.

While the still-uncertain economy is one of the best reasons to revisit the capital investment process, there are other compelling forces at work as well. Today, manufacturers are pursuing a number of strategies to achieve growth and success, from mergers and acquisitions to new moves into emerging markets. All of these strategies share a common need to maximize efficiency in the way that capital is deployed. Merged organizations need to optimize their footprint and manage their shared assets. Companies moving into new markets need to invest in local production capacity in order to achieve growth objectives and service local demand, and need to do so with lower capital intensity than within mature markets.

Changing the way that major equipment purchases are made is not easy, but the savings are real and measurable. Aligning the math with the mission of achieving efficiency requires a commitment to revisit some well-established systems that are often resistant to change.

In short, old business habits in the area of procurement could be costing you points on your margin, and so embracing a new approach should be order of the day. Making the leap to better equipment procurement involves not just a revision in capital acquisition procedures, but also a revision in the way that your business perceives the role of procurement itself.

Instead of seeing it as a simple transactional moment near the end of a decision to buy a particular piece of equipment or service, manufacturers should view procurement as an essential, integrated part of the process. We call it the “New Procurement.” Ultimately, to achieve maximum spending control and savings, the procurement of any product or service within your organization should abide by the same procedures and principles. Smart buying decisions require upstream coordination and planning across departments, deep market intelligence, knowledge of how to source material, understanding of commodities pricing and experience in the area of energy efficiency credit management. Oftentimes, an outside specialist can be a key asset in ensuring all these elements come together.

With these elements in mind, here are some key considerations to help get equipment purchasing in gear:

Re-Engineer the Process from Beginning to End … & Beyond

All too often, the decision to acquire a particular piece of equipment, and the ensuing sourcing decisions, is disconnected from other capital investment decisions. Simply put: it lacks strategy. As a result, your company cannot leverage its buying power in order to attain the best value and the strongest contract terms.

In many cases, significant dollars are lost in translation between the staff at the plant, including the engineers who manage the equipment, and those finally responsible for procurement. When sourcing decisions are made infrequently — and when the same sources are used out of habit time and again — you may get the right equipment, but at the wrong total cost of ownership. Without a broader understanding of the market and supply base across all geographic areas, the people in your organization who guide equipment decisions and sourcing may have the right motives, but they lack the right information to maximize your savings. Simply put, engineering departments have the technical knowledge necessary for capital acquisitions, but they often have little time or capacity to engage in rigorous strategic sourcing and contracting.

At the same time, multiple equipment buys may be planned in different plants at the same time, with no coordination and planning between them. In many cases where capital acquisition is occurring across departments and regions, manufacturers miss clear opportunities to negotiate better cost structures and terms through well-defined master service agreements.

The first step in fixing this costly problem is to re-engineer the process and re-envision the role of procurement. Your procurement department, including staff and advisors and outside consultants, must function as an active and integrated stakeholder in the organization. They should be involved in purchasing decisions across the company, from beginning to end — and beyond — to the management of contracts. And this integration must happen upstream in the capital planning and budgeting process. By adopting a more holistic approach to capital spending, where both technical expertise and market knowledge are brought to the table and coordinated company-wide, you can generate consistent savings.

Emphasize the Value of Contracts & Contract Management

You have heard the stories before, and may have experienced the problem yourself. A critical and valuable piece of machinery is purchased at a fair price, but recurring performance issues, persistent maintenance problems and costly spare parts have severely diminished what once looked like a good deal.

The fact is, a successful acquisition does not end with expert sourcing and the negotiation of a competitive cost structure. Arranging robust contracts for performance and maintenance is critical to achieve real value. In fact, to understand the true cost of ownership, factoring in expenditures for repair and upkeep, is clearly essential. Experienced contract negotiators can drive down the true cost dramatically by insisting upon and obtaining performance guarantees and positive terms for maintenance. A new approach to equipment purchasing in the New Year means that this often overlooked piece of the procurement puzzle must be addressed.

Understand & Aggressively Pursue Energy Incentives

When it comes to equipment procurement, the opportunity for energy efficiency (EE) incentives is broad. The savings that these incentives promise is not only quantifiable, but it should consistently inform and guide overall acquisition decisions and project choices. In 2010, 47 states included funds for EE, offering more than $7.5 billion in loans, rebates, grants and general education and outreach campaigns designed to reduce energy use. By 2020, this pool of funds is expected to increase to as much as $12 billion. Even with state budget cuts, EE funding is expected to increase substantially, because the cost of subsidizing energy reductions is lower than the cost of building new capacity.

Given the numbers, a greater focus on EE must be a central part of your new procurement strategy. Finding and pursuing the many incentive programs is complex, but since cash incentives can reduce project costs by as much as 50 percent, the outcome more than justifies the effort. Developing a procurement team that can consistently deliver incentive dollars is therefore critical, and specific experience in the EE area should be emphasized. Many custom, negotiated incentive programs require measurement and verification (M&V) of energy savings, and the procurement team should have the ability to manage this process.

Prioritizing energy efficiency, of course, brings other valuable benefits. By strategically engaging in purchases that follow EE protocol, organizations can more efficiently allocate capital investments, while at the same time allowing them to demonstrate to employees, investors and others a commitment to reducing carbon emissions. In fact, through innovative reporting tools like Energy Efficiency Credits (EECs), you can communicate your progress toward sustainability goals more easily to a variety of audiences.

Understand the Hidden Costs & Risks

Capital acquisitions, large and small, involve numbers — and all the numbers should count when the final decisions are made. Understanding not just the cost of a particular product, but also the commodity pricing models that inform it, is essential. Deep market intelligence means understanding the role of emerging markets in equipment production and basic material supply, for instance, in order to find and accurately evaluate the best sources.

When manufacturers discuss efficiency, they often relay their desire to remove waste and excess in the production process, and in administrative and oversight functions. In the area of procurement, efficiency involves not so much the removal of waste — although wasteful spending is eliminated with good procurement practices – but instead the removal of uncertainty. With an effective process in place for capital acquisitions and procurement in general, manufacturers should be assured that every variable has been considered, researched and understood, and that the process will proceed quickly and smoothly and result in savings through the reduction of the total cost of ownership that considers the full life cycle costs of the acquisition.

Building this new procurement system can occur in different ways. Some organizations create significant in-house departments, while others turn to outside specialists dedicated to understanding and guiding all of the elements of the task of purchasing and managing products and services.

Although the four key aspects highlighted above provide a very good start in rethinking the procurement process for your capital investments, this is not necessarily an exhaustive list. Ultimately, to get your capital spending in order, there is no better place to start than with getting your company's procurement team and process in gear.

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