ARGO CONSULTING

Capital Equipment Manufacturer Uses Procurement Improvement Process to Leverage Growth and Reduce Material Costs 5%

September 2020

The Situation

A Private Equity owned manufacturer of capital equipment was experiencing significant growth from both acquisitions and organic growth. Our client is viewed as the premier supplier of this type of capital equipment in an industry with many entrants. Barriers of entry to this business are not significant so cost and service are viewed as critical to achieving and maintain market share. Generally, incumbents enjoy repeat business from existing customers. The acquisitions (from a procurement perspective) were not integrated into the enterprises processes and volume synergies were not being explored. As a result anticipated cost reductions were not being achieved.

Our client was looking to leverage the total enterprise spend, increase the professionalism of the procurement group and realize the synergies that have been presented due to acquisitions.

Argo's Solution and Implementation

The initial step was to execute a four-week deep dive analysis to identify the opportunity and develop an implementation plan.

PROCUREMENT OBSERVATIONS

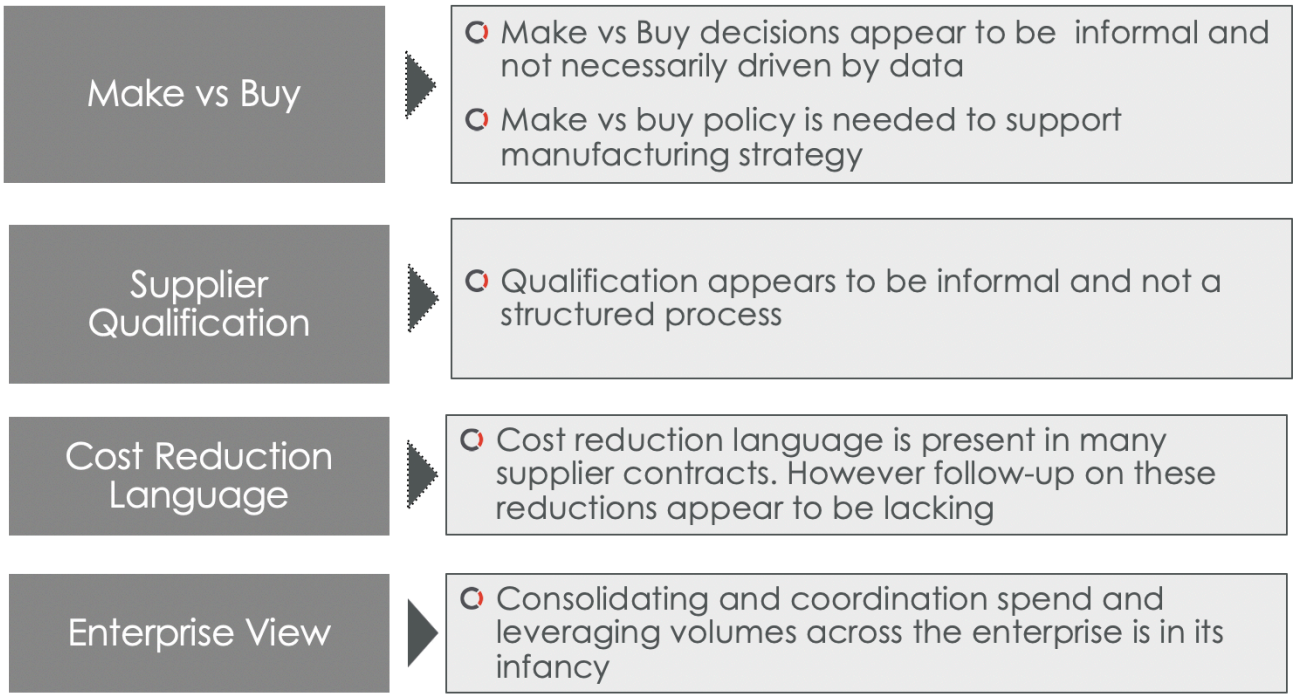
VMI
- Current VMI could be enhanced. Both with current and new suppliers
- Suppliers need to shoulder more of the load

Metrics
- In the absence of performance-based metrics decision making may be compromised
- Supplier performance criteria and reviews need be developed and implemented

Data
- Data availability and fidelity is encumbering the performance of the procurement folks
- In the absence of quality data tribal knowledge will prevail

Industrial Distribution
- A significant spend $5.5 million is with distribution. This should present an opportunity

LCC Sourcing
- While volumes are generally not attractive to LCC opportunities. We will explore the possibilities on a few commodities.



Key Findings

Spend Consolidation and Supplier Rationalization While many of the "commodities" being purchased were common between multiple facilities, the number of common suppliers being used to service multiple facilities was very low.

Procurement not Viewed as Strategic Most of the procurement activity was viewed as tactical and not strategic. Most of the purchasing activity was performed as individual purchase orders, and volumes (both local and enterprise) were not being leveraged.

Softening Commodity Pricing The client was able to recognize softening commodity pricing and was able to achieve some significant cost reductions. However, the same strategy needed to be employed to all purchased components that that have the softening commodity prices as part of their cost structure.

Enterprise Coordination Among the procurement leads at the facilities, enterprise coordination needs to be enhanced. Strategies need to be discussed and agreed upon. Spend consolidation needs to be implemented and executed. Commodity management methodology needs to be implemented.

Contractual Language Current contract language needs to be strengthened. Cost reduction language needs to be incorporated, as well as performance improvement and most favored nation language.

Common Supplier Spend

There was limited coordinated spend across the enterprise, with:

- Two suppliers serving all four facilities
- Four suppliers serving three of four facilities
- Twenty-one suppliers serving more than one facility

Supplier	Site 2	Site 1	Site 4	Site 3	Count	Total Spend
Supplier 1	$1,550,999	$780,905			2	$2,331,904
Supplier 2	$552,983		$492,010	$76,276	3	$1,121,269
Supplier 3	$67,000	$971,176			2	$1,038,176
Supplier 4	$128,211	$753,104			2	$881,315
Supplier 5	$69,594	$67,143	$678,478		3	$815,216
Supplier 6		$44,210	$735,079		2	$779,289
Supplier 7	$6,325	$754,275			2	$760,600
Supplier 8	$120,388	$518,681			2	$639,069
Supplier 9	$68,670	$500,281			2	$568,951
Supplier 10			$492,061	$76,277	2	$568,338
Supplier 11	$472,742		$87,191	$127	3	$560,060
Supplier 12	$154,843	$390,776			2	$545,619
Supplier 13	$485,630	$33,750			2	$519,380
Supplier 14			$406,921	$31,555	2	$438,476
Supplier 15	$171,271	$267,030			2	$438,301
Supplier 16	$5,163	$356,337			2	$361,500
Supplier 17	$48,978	$302,883			2	$351,860
Supplier 18	$6,321	$309,083			2	$315,405
Supplier 19	$106,597	$87,067	$41,072		3	$237,046
Supplier 20			$11,185	$213,442	2	$224,627
Supplier 21	$23,522	$171,005			2	$194,526
Supplier 22			$177,176	$5,986	2	$183,161
Supplier 23	$90,082	$2,035	$79,257	$468	4	$171,842
Supplier 24	$20,789	$26,038	$115,002	$1,975	4	$163,804
Supplier 25			$30,331	$70,004	2	$100,335

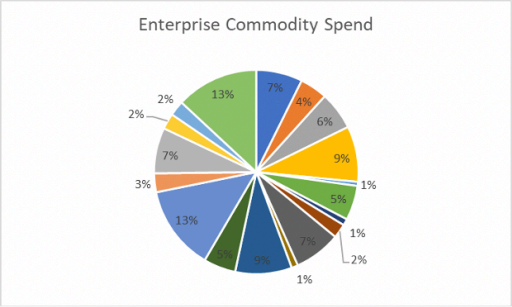
$100,000 and above

Commodity Spend

Commodity	Site 1	Site 3	Site 4	Site 2	Total
Aluminum Castings/EXT	$115,261	$649,718	$223,865	$3,547,023	$4,535,867
Brushes and Foam	$907,395			$1,784,300	$2,691,695
Controls	$868,057	$438,072	$1,183,777	$1,242,120	$3,732,026
Drives Motors	$1,757,219			$3,694,976	$5,452,195
Vacum	$332,453			$62,775	$395,228
Electrical Comp	$836,206	$129,516	$912,127	$1,511,402	$3,389,251
Fans	$116,093			$518,894	$634,987
Fasteners			$932,348	$465,540	$1,397,888
Fluid handling	$1,023,838			$3,547,823	$4,571,661
Graphics		$298,869		$334,131	$633,000
Industrial Dist	$1,222,245		$3,637,450	$676,906	$5,536,601
Lighting		$1,016,126	$677,607	$1,455,750	$3,149,483
Logistics		$276,613	$1,752,481	$6,252,849	$8,281,943
Lumber		$401,450	$224,434	$1,219,253	$1,845,137
Machined and Fab	$1,515,878		$1,285,461	$1,675,341	$4,476,680
Paint	$685,400			$859,535	$1,544,935
Plastics	$269,144	$663,103	$321,298	$231,647	$1,485,192
Steel	$796,049	$862,574	$3,619,587	$2,795,100	$8,073,310
Grand Total	$10,445,239	$4,736,040	$14,770,435	$31,875,365	$61,827,078

- Commodity management structure and process needs to be implemented
- Detailed commodity associations need to be set in place for accurate data analysis and decision making

- Commodity analysis and understanding is paramount in a successful strategic sourcing exercise.
- Knowing what is purchased and where it is coming from is critical



Procurement Cost Savings Opportunities

Commodity savings need to be leveraged to the component level

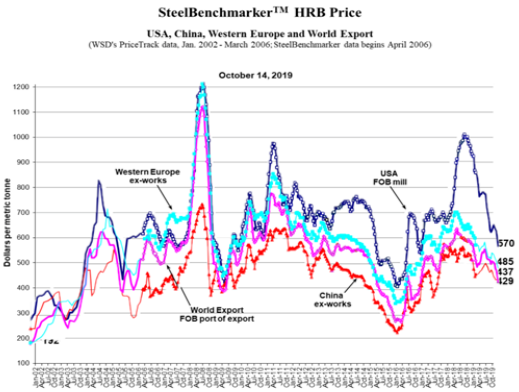
Commodity	Projected Spend	Executed Savings	Savings % of Spend
Raw Material	$5,791,576	$1,441,720	24.89%
Chemicals	$7,390,744	$208,837	2.83%
Machining/Metal Fab	$4,476,680	$91,021	2.03%
Powder Coating	$1,544,935	$217,420	14.07%
Totals	$19,203,935	$1,958,998	10.20%

- Good work capitalizing on a softening materials market
- Softer materials market should have generated greater savings in Maching and Metal Fab

Facility 2 Raw Material	
Volume at Standard	$2,795,099
Volume at New Pricing	$2,461,590
Delta (savings)	$333,500
Percentage Savings	11.93%

Facility 1 Raw Material	
Volume at Standard	$3,619,586
Volume at New Pricing	$2,496,975
Delta (savings)	$1,122,612
Percentage Savings	31.01%

ALUMINUM IN USD – HISTORICAL PRICES



Projected Saving Potential

With an increase in bandwidth, concentrated effort, project management, and professional guidance, we found the following potential cost savings range of 3% to 5% material spend :

Corporate Commodities	Est. Spend all facilities	Potential %		Potential Range		Rational
Metal Raw Material	$5,791,576	1%	4%	$57,916	$231,663	Reevaluate some items
Machining/Metal Fab	$4,476,680	3%	6%	$134,300	$268,601	Left something on the table
Electrical	$4,031,373	4%	6%	$161,255	$241,882	Copper chart
Valves/Fittings	$4,571,661	4%	7%	$182,866	$320,016	Steel bronze and aluminum
Pumps	$2,812,385	2%	4%	$56,248	$112,495	Cast housings or machined
Electronics/Displays	$3,732,026	3%	5%	$111,961	$186,601	Copper, aluminum and LCC
Fans	$634,987	1%	3%	$6,350	$19,050	Steel (Captive product)
Motors	$5,452,195	4%	7%	$218,088	$381,654	Aluminum, steel, copper, volume
Cylinders	$858,910	3%	5%	$25,767	$42,946	Steel
Lighting	$3,149,483	4%	8%	$125,979	$251,959	Copper, aluminum and LCC
Casting	$4,535,867	4%	6%	$181,435	$272,152	Scrap pricing
Fiberglass/Grading	$592,569	2%	6%	$11,851	$35,554	Fiberglass pricing relatively flat
Industrial Distribution	$5,500,000	8%	15%	$440,000	$825,000	Move to manufacturer
	$46,139,712			$1,714,016	$3,189,573	

Dec — Projected Savings Timeline — Oct

During the implementation, the COVID-19 pandemic caused global supply chain disruptions. Argo orchestrated and implemented a risk mitigation assessment to determine and predict where disruptions may or could occur. Once the assessment was completed risk mitigation plans were developed and implemented.

Risk Assessment Summary

Procurement Risk Management Site 2												
Number of Items	Item Description	Supplier	Supplier Address	Supplier Ship From (If Different)	Ownership Structure (Public or Private)	Company Size	Schedule Risk	Financial Risk	Relative Position	Over all
9	Cylinders	Supplier 1			Private	1	3	4	3	
16	Reducers	Supplier 2			Private	2	2	3	2	
Procurement Risk Management Site 4										
Number of Items	Item Description	Supplier	Address	Ship From if different	Ownership structure (Public or Private)	Company Size	Schedule Risk	Financial Risk	Relative Position	Over all
	Contract Mfg	Supplier 1			Private	1	2	2	2	
	Machined Components	Supplier 2			Private	1	2	3	2	
	Fluid Power	Supplier 3			Private	1	3	3	3	
	Rotational Molded	Supplier 4			Private	1	2	3	3	
Procurement Risk Management Site 1										
Number of Items	Item Description	Supplier	Address	Ship From if different	Ownership structure (Public or Private)	Company Size	Schedule Risk	Financial Risk	Relative Position	Over all
	Motors	Supplier 1				1	2	4	3	

Risk Assesment Summary							
		Overall Rating					
		Green		Yellow		Red	
Facility	Number of Suppliers	Number		Number		Number	
Site 4	16			12		4	
Site 2	18	1		15		2	
Site 1	27			26		1	
Site 3	0			0		0	
Total	61	1		53		7	

1) Is what I thought when I put together this assessment still valid? If not what needs to change.
2) Are there items/companies that should be removed from the "risk" category?
3) Are there changes that are occurring either economically and/or geopolitically that would cause me to add items or companies to this risk assessment?
4) Are there changes that have occurred that need to be elevated to senior management?
5) For those categories that we did not have good data and had to estimate (financial for example) we should work to get more granular data moving forward.

Argo filled an interim procurement lead position at the client and implemented a process that aligned all the procurement leads and developed a sourcing plan that assigned individual leads specific commodities and responsibilities. Argo also aligned strategic and tactical procurement functions and developed roles and responsibilities for each function. We then developed a strategy for each commodity and an implementation plan. Finally, we developed metrics to track progress.

Summary

Argo was able to exceed (on the high side) a savings target greater than 5% of material spend of our original assessment of the savings opportunity. We were able to do this by deploying various procurement strategies. The managed competition strategy for raw materials was the most successful and produced the largest savings. The split manufacturing strategy (essentially a make vs buy) also provided significant savings. Supplier changes and negotiations also provided additional savings. In addition, the client was left with a process that can be used to generate additional cost reductions going forward.

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