E-SOURCING FORUM



# MRO Cost Drivers Must be Solved in Order to Control Cost

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MRO is an acronym for Maintenance, Repair and Operations parts and supplies - materials and services that do not go directly into the end product. MRO is used by the plant to maintain, repair or operate the machinery and processes used in the actual manufacturing activity.

- U.S. manufacturers spend approximately 55% of total revenue to purchase goods, services and capital equipment.
- Approximately 20% of these purchases are for indirect materials or MRO.

In projects completed by **Paladin** there are similar operating characteristics in these manufacturing locations. Typically, MRO operations:

- Generate numerous low-dollar unplanned buys.
- Include a high amount of slow moving MRO inventory.
- Lack commodity management concepts and processes which can generate significant operational advantages and cost reductions.

This is an area in which Manufacturers fail to control spending for the following reasons:

- MRO viewed as tactical (keep the plant running), not strategic
- Wide diversity of sourcing skills required due to the number of MRO categories
- Lack of strategic Purchasing support
- Heavy reliance on personal relationships with suppliers
- Priority on fast delivery, not best price

- Inadequate information systems for ordering and requirement specifications
- Inadequate performance measurement processes
- Too many vendors not online, resulting in small order volume
- Heavy reliance on personal relationships developed over a number of years

This lack of controls can be categorized into MRO cost drivers and potential solutions.

| Cost Driver | Solution |
|---|---|
| Lack of knowledge about the purchasing and payment process | Spend Analysis to develop an understanding of major commodities and buying patterns. The data can be used to identify cost reductions and value added services. |
| Decentralization of MRO purchasing & failure to generate leverage in the supply base | Centralize or coordinate the buy if Spend Analysis identifies multiple buyers across manufacturing locations with different prices or terms |
| Failure to understand that cost drivers are a major contributor to poor cost management and control<br>Causes include:<br>1) Lack of sufficient training and<br>2) Budget or Accounting systems that divide costs and cost control among different operational units. | Create commodity teams to identify and model specific cost drivers for research, training and control |
| Poor relationships with suppliers | Provide information to suppliers and include them in research and plans. Incent suppliers to share product and market knowledge. |

Businesses have not focused on reducing indirect costs like MRO which operated as fiefdoms and were untouchable because of their charter to “keep the plant running”. Now managers are realizing that the business must also identify the major MRO cost drivers in order to get MRO costs under control.

**Paladin Associates Inc.** has managed MRO e-Sourcing events, evaluated MRO spend and suppliers, facilitated contract negotiations and assisted in the implementation of solutions which realized significant savings for clients.

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**Paladin Associates Inc.** a Sourcing Cost Reduction firm, offers strategic sourcing expertise for multiple commodities to secure “fast track” quantifiable savings and long term cost reduction programs.

We can help you with technology implementations such as spend analysis and eSourcing as well as sourcing process improvements, skill training and staff development while delivering bottom line savings with a guaranteed ROI.\

For more complete information, visit: **http://www.PaladinAssociatesInc.com**