

Magnetics: Industry Overview

Global Auctions in the Magnetics Industry

by *Walt Benecki*

Ready or not, you must prepare for the market's transition to e-sourcing and the reverse auction

Billions of dollars worth of products and services have already been purchased using reverse auctioning techniques. It is clear that the first decade of this century will see a virtual explosion of change in how companies conduct business. Some of those in the forefront of this new purchasing phenomenon include United Technologies, General Electric, Dana, Siemens, Danaher, Valeo, Texas Instruments, BMW, Cisco Systems and Visteon. It is estimated that well over \$100 million of our industry's products were purchased during 2001 utilizing reverse auctions. The value of magnetic products auctioned off this year could accelerate to \$400-500 million. Magnetic producers, as well as manufacturers of motors, sensors, transformers and power supplies, will find themselves participating in this new process, whether they want to or not.

The reverse auction is a process that culminates with multiple suppliers bidding their price level online during a 30-45 minute time window. The electronic auction not only provides purchasers with significant cost savings, it has the potential to reduce purchasing cycle time. Price reductions of 15-25% are routinely being reported. In 2001, Danaher auctioned off a \$22 million permanent magnet spend and subsequently reported a 27% savings (\$6 million). Numerous companies have reported cycle time reductions in the range of 15-30%.

The leading supplier of software, training and related services for e-sourcing is FreeMarkets, Inc. (www.freemarkets.com), headquartered in Pittsburgh, PA. A recent industry survey by the Aberdeen Group ranked Ariba Inc., Sunnyvale, CA (www.ariba.com) as the second most preferred e-sourcing vendor to industry. General Electric has developed in-house e-sourcing capability, but most companies have chosen to outsource the technology to save time and manage start-up costs.

Buyers can quickly achieve a global reach and identify low cost producers, worldwide. Of interesting note is the fact that second time savings are often greater than experienced in the initial auction. This is the result of more supplier acceptance of the process, improved supplier capability, new

qualified suppliers, and technology improvements. The process is also impacted by market dynamics and economic conditions which may influence suppliers' aggressiveness.

There are also some significant supplier advantages related to e-sourcing. Suppliers are forced to focus on their own cost reduction initiatives and incremental volume is available to those who achieve low cost producer status. The bidding process provides instant feedback regarding competitive bids and the resulting market price of their products. It is also possible to walk away with longer term contracts and business is sometimes split between the two bidders offering the best value.

There are pitfalls for both buyers and sellers. Buyers without solid top management support will fail as they navigate against internal resistance to change. Inconsistent or unethical practices such as permitting unqualified bidders to participate in the auction can turn away valued suppliers. Unreasonable terms and conditions can also discourage highly qualified potential bidders. Specifications must be up to date. It is important to note that just because a new magnet vendor "meets the spec", this does not assure that a vendor transition will be smooth. I have personally observed cases where the transition to a new vendor's magnet (meeting the specifications) resulted in unacceptable performance in the final device or where attachment and/or excessive breakage problems were suddenly encountered in automated assembly systems.

Sellers must shed the emotion associated with reverse auctions and do considerable preparatory homework. Specifications must be scrutinized, but the first priority must be to know your costs! The temptation to succumb to a "low bidder" mentality must be overcome. E-sourcing advocates report that 30-50% of the "low price" bidders do not prevail. Value will continue to influence final sourcing decisions.

E-sourcing will be a strategic business driver throughout this decade. At a recent FreeMarkets conference, Kent Brittan, Vice President, Supply Management for United Technologies reported, "Supply Management is becoming a UTC core competency". Kenneth Way, Chairman of Lear Corporation said, "Without doing e-commerce, we will not survive". New multilingual desktop software now guarantees that global e-sourcing will be a normal part of the business process, not an occasional tactical event.

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