Contain Construction & Remodel Costs

Getting Creative at the Tier 2 and 3 Purchasing Level

When a construction management team indicates the cost of a construction or remodel project is soaring, design teams often act quickly. Cut out this feature, slice that curve, trim the quality of specific material.

On large remodel programs this is a painful endeavor with many risks. Slicing unique features at your facility can cost dearly in the long run. Reducing size can affect your future growth plans. Given today's climate for more corporate social responsibility, low quality substitute materials are not the best way to approach this issue.

Intelligent sourcing of tier 2 and 3 construction materials can provide a large portion of the budget solution and can be socially rewarding.

Sourcing Tier 2 & 3 Construction Materials

Program Example

The design team on a 1,000 unit multi-year remodel program decides to include a metal panel and trim package as a small portion of a $300,000 per location remodel.

On the job, the metal panel and trim material costs the owner $5,000, or roughly 1.5% of the overall cost of the remodel. On 1,000 units, the total cost of this multi-year specific material purchase would be $5,000,000.

The process for determining which trim and panel to use occurs during the design phase. It is at this point that designers and purchasing agents should be exploring Tier 2 and 3 purchasing agreements.

Examining the Supply Chain

The owner is buying the material from a general contractor, which carries a markup of 5%.

The general contractor is buying the metal as part of his roofing bid. This carries a markup of 10%.

The roofer is buying this material from a material distributor. This carries a markup of 10%.

The distributor buys from a local sales rep. This carries a markup of 10%.

The pricing from the local sales rep is based on 1 unit, not 1,000 units, carrying an additional 10%.

45% or more *of the spend at this tier 2 or 3 category adds no value to the project.*

Tier 3 Purchasing Agreement

In this real world example, during the design phase, the prototype team involved the manufacturer and purchasing team. A tier 3 purchasing agreement was then signed by the manufacturer.

The spend is now fixed at a lower level, ensuring the roofer buys the material at the lowest price. The costs are visible, and lead times are ensured, however the owner leaves purchasing, installation, warranty, and quality in the hands of its lower tiers of the chain.

The manufacturer receives better information on potential volume and timing and can better support the program with inventory and staff. The manufacturer also has a vested interest in a 1,000 unit program versus a single project they cannot see in their normal delivery model.

Low Risk Execution

In this specific case, a tier 3 buying agreement results in 2 million dollars of savings and very little management on the part of the procurement department. An additional 8 remodels can be completed with the saved dollars, and no additional purchasing risks have been encountered since the buying remains at the tier 3 level.

Steps to Capture Value

In some of the most effective organizations, their purchasing excellence shines in a few specific areas:

Savings Uncovered During Design

When team members involve strategic or national account departments at the manufacturer level the supply chain is uncovered quickly. Will installing contractors buy directly or will their subs buy? Are they buying through a distributor? Is there a better way to get the product to the site on time? Savings are identified during design by asking supply chain questions.

Procurement Purchasing Agreements

Procurement is capable of assembling tier 2 and 3 vendor agreements on products the design team selects through simple purchasing agreements. Low commitment, low management pricing agreements designed to shorten the supply chain while keeping the purchasing risk at the tier 2 or 3 level are an integral part of controlling costs.

Lead Time

The procurement team incorporates lead time reduction in the purchasing agreement which reduces costly delays during construction projects and remodels. This consistent lead time is an exceptional benefit to material manufacturers and can be utilized to negotiate better pricing.

Multi-Location Buying Power

Using the buying power of a multi-location remodel or new construction program without forcing the direct management of a small dollar item per location purchase can ensure high quality products while reducing spend.

Measuring Total Spend

Reporting on total expenditures falls on the manufacturer. Spend reporting in a tier 2 or 3 category is made the manufacturer's responsibility in the purchasing agreement. What gets measured improves, and measuring total spend at the tier 2 and 3 category is a vital piece of controlling quality and cost.

Corporate Social Responsibility

Incorporation of Tier 2 and 3 spending programs into MBE/SBE goals is a significant way to increase MBE/SBE participation. Reporting of tier 2 and 3 spend in a remodel or construction program benefits your company financially and it often diversifies your spend at the small business and minority level. Many more MBE/SBE vendors now have a better opportunity to participate.

Are you grabbing the tier 2 and 3 value during your construction or remodel program, or are your teams overlooking this strategy? It is easier than you may think to uncover the supply chain and capitalize on your buying power, making it both socially and fiscally responsible purchasing.