



*The Institute for Supply Management's 67<sup>th</sup> Semiannual Economic Forecast ranked energy supply costs as the top two economic concerns of purchasing executives surveyed. Executives seeking to realize significant operational cost savings would do well to review their company's energy supply procurement policy. By utilizing effective e-procurement methods and soliciting competitive bids from multiple suppliers, companies can save as much as 20% on energy supply costs and realize staggering financial returns with an average payback period of less than one month. [Editor's note: ISM's December 2007 Semiannual Economic Forecast further cited that executives in the manufacturing sector report their top economic concern as "energy cost and supply"; their counterparts in non-manufacturing industries similarly cite "high energy, fuel and transportation costs" as their number one economic concern.<sup>1</sup>]*

## Energy e-Procurement Offers Exceptional Financial Returns

By Dr. Jack Mason, President, EnergyWindow, Inc.

Driving down operating costs is crucial to competitive success. Once the low-hanging fruit has been picked, however, identifying meaningful savings opportunities becomes increasingly difficult. Where can executives look to find the kind of savings that can significantly improve the bottom line?

Energy supply. Expenses for natural gas and electric energy supply are among many business' top expenses, and for a retail chain, can easily soar into the tens, or even hundreds of millions of dollars. Energy supply costs rank high on the list of executive's concerns when it comes to cost-containment. In fact, purchasing and supply executives surveyed for the Institute for Supply Management's 67<sup>th</sup> *Semiannual Economic Forecast* ranked them as the number one economic concern in the non-manufacturing sector and number two in the manufacturing sector.<sup>2</sup> Still, energy supply costs are often overlooked or under-served. Even a modest savings of a few percent versus regulated rates can have a real impact on the bottom line.

The means by which many retailers and other concerns are able to achieve significant savings is to take facility energy supply needs to the competitive market, where suppliers bid to win the energy contract. In states where energy is deregulated, electric and gas market suppliers can present buyers with meaningful savings opportunities with low risk. More than a dozen states and provinces have competitive electricity markets, and many more than that have competitive natural gas markets.

Consider the following real-world example shared by EnergyWindow, a leading reverse auction energy e-procurement provider:

A large, national retailer determined that it had electricity and natural gas supply needs representing approximately \$37 million at tariff price. The retailer operates facilities in several different states that have competitive energy markets and elected to enlist an energy e-procurement specialist to identify active markets and available suppliers, gather necessary historical data, post individual requests for quotation (RFQs), and solicit bids. The retailer identified winning bids and negotiated contracts directly with those suppliers. As a result of their efforts, the retailer saved \$9.5 million (or 26%) off the tariff supply price, representing a corporate bottom line reduction of 1.0 cents per share, per year, over the three-year energy contract period.

<sup>1</sup> December 2007 *Semiannual Economic Forecast*, <http://www.ism.ws/about/MediaRoom/newsreleasedetail.cfm?ItemNumber=17369>

<sup>2</sup> 67<sup>th</sup> *Semiannual Economic Forecast*, "Economic Concerns," Institute for Supply Management, <http://www.ism.ws/ISMReport/SemiannualROB042004.cfm>

Supply executives place strong emphasis on improving and expanding applications for e-procurement.<sup>3</sup> In recent years, e-procurement methods have made seizing gas and electric savings opportunities easier and faster than ever before. Just as businesses can purchase computers and MRO supplies online, they can now purchase energy to fill short- and long-term needs. Because these methods can reduce by more than a factor of 100 the effort and cost of pursuing competitive energy bids, the return on investment can be extremely favorable.

EnergyWindow offers compelling evidence to illustrate this. The results in the table illustrate the range and average of energy contracts resulting from e-procurement on their web site during the last two years. The table below provides the basic contract parameters and some typical financial project performance measures.

	Largest Contract	Average Contract	Smallest Contract
# of Facilities	55	23	3
Contract Term (months)	36	18	12
Value	\$23,773,000	\$1,996,000	\$375,000
Savings	\$9,111,000	\$505,000	\$11,000
Effort invested (staff hours)	120	10	3
Cost of initial investment	\$18,000	\$1,500	\$450
Net Present Value	\$7,043,667	\$363,946	\$7,926
Internal Rate of Return	8,431%	22,394%	2,344%
Simple Return on Investment	49,900%	33,567%	2,344%
Discounted Return on	39,031%	24,163%	1,661%
Payback period (months)	1	1	1

NOTES: Loaded hourly costs = \$150  
Discount factor/cost of capital = 15%  
Minimum payback period is one monthly billing cycle.

If you choose to buy energy via an e-procurement exchange, an aggregator or a reverse auction, you should shop around to determine whether or not the provider is well equipped to handle the unique area of energy procurement. A good energy e-procurement partner should possess the following:

**Tools and energy expertise.** Energy markets are complex and change rapidly. A good energy e-procurement provider should have the necessary resources to help you capture more of the available savings opportunities than if you were acting on your own, and do so more quickly and at lower total cost. Access to a pool of active suppliers as well as in-depth market and regulatory information is key to helping you react quickly when conditions for purchase are favorable.

**Rigor.** Before the first RFQ is generated, a good energy e-procurement provider should help you research where savings opportunities exist, as well as convey deep understanding of the relative benefits of various types of contract structures at any given time. If the provider is knowledgeable, they should be able to tell you what the market trends are and what duration and type of contract may

<sup>3</sup> 67<sup>th</sup> *Semiannual Economic Forecast*, "Supply Chain Practices in 2004," Institute for Supply Management, <http://www.ism.ws/ISMReport/SemiannualROB042004.cfm>

be best worth considering. In the end, the approach should produce an “apples-to-apples” comparison of supplier offers that is auditable and a decision that is easy to explain to upper management.

**Transparency.** Some broad-based e-procurement providers don't allow buyers to interface directly with suppliers. With energy e-procurement, it's crucial that buyers and suppliers can communicate freely and directly with one another in order to obtain the best quality information and thus achieve the lowest possible price. Transaction fees and terms should be clearly disclosed up front.

**Objectivity.** Look for a provider that is independent of energy supplier or distributor influence. You want to feel comfortable that the provider is truly working to help you find the best deal and that there are no conflicts of interest.

**Customer service.** Energy e-procurement involves very high-dollar transactions and consideration of many complicated options. When you have questions, you want to be able to consult with a highly-informed industry veteran who can help you think strategically about your purchase, not just help you fill out online forms.

**Supply chain consistency.** Energy procurement activities can and should be consistent with your overall supply chain strategy, procurement approach, and business priorities. If you have invested in an enterprise e-procurement system, you should choose an energy e-procurement provider that can and will work to leverage your existing system, when appropriate.

If your company is not already purchasing energy via e-procurement, consider the advantages of moving in this direction. E-procurement enables you to post your energy supply needs more quickly and efficiently, simultaneously distributing requests for quotation (RFQs) to multiple suppliers. Working with a provider that specializes in energy transactions and understands the complexities of natural gas and electric markets carries the added benefit of helping you capitalize on more savings opportunities than you might be able to if you choose to go it alone.

*EnergyWindow is a Boulder, Colorado-based company that offers a comprehensive suite of information technology-based tools and extensive energy industry expertise to help businesses manage every element of their energy supply cycle. Specifically, EnergyWindow offers: an online request/bid system for energy procurement; a real-time, online energy market database that tracks the best opportunities for energy procurement; an energy management information system that allows energy managers to track and analyze their company's energy usage; and energy supply strategy and management consulting. The company can be reached at [www.energywindow.com](http://www.energywindow.com).*