Huntington | TECHNOLOGY FINANCE

# Recommendation to Business Executive Leadership on Endpoint Cost Management

MONTH 00, 2018

# Recommendation

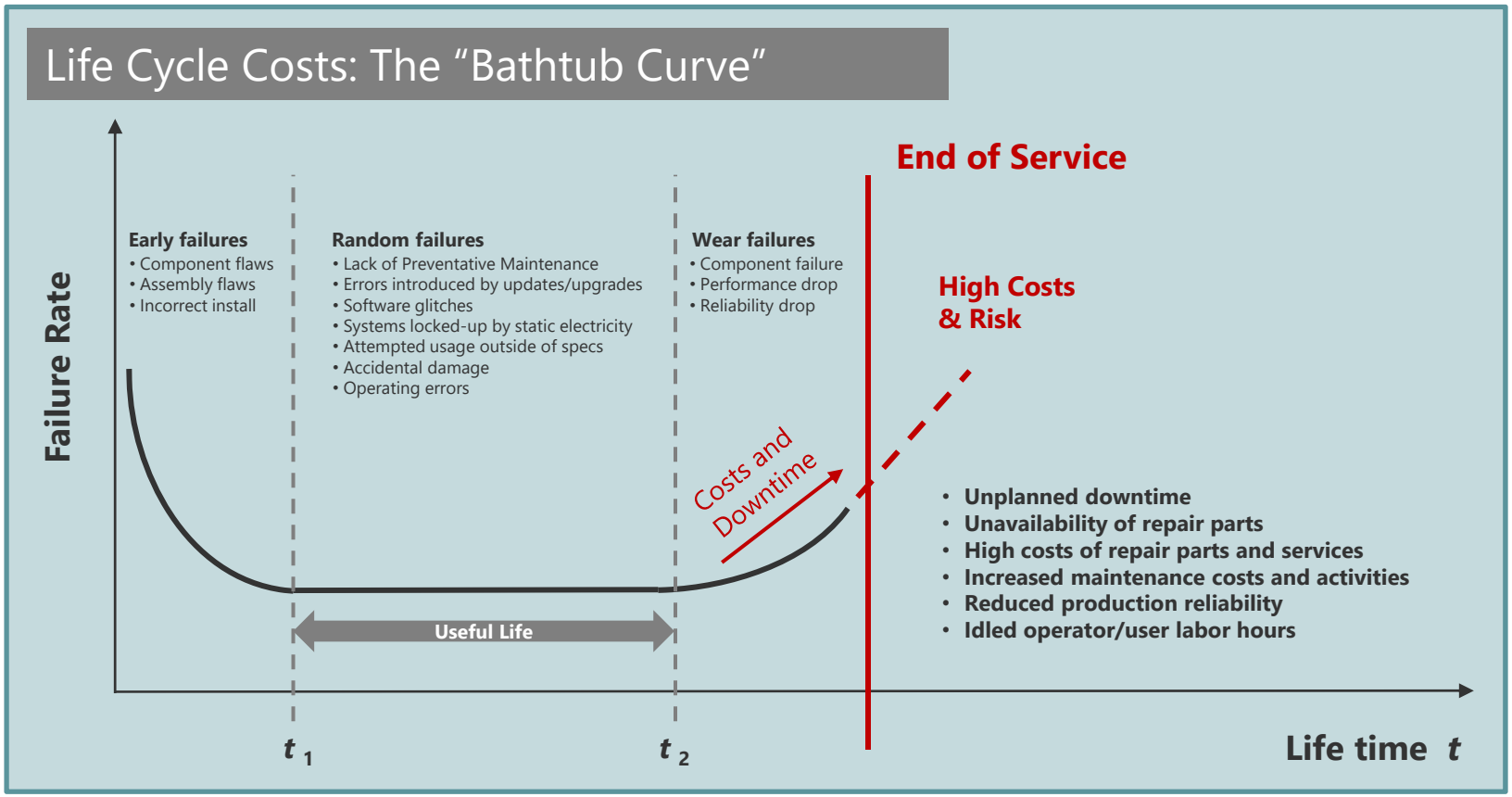
Because lifecycle costs for end-user computing devices are excessive after the manufacturer's warranty period, Central Supply Chain Management (SCM) should be asked to explain:

1. **What the refresh cycle is for such assets**
2. **How that cycle is determined**
3. **How those assets are treated differently from other assets**
4. **How TCO (Total Cost of Ownership) and LCCM (Life Cycle Cost Models) are used in setting refresh timing policy.**

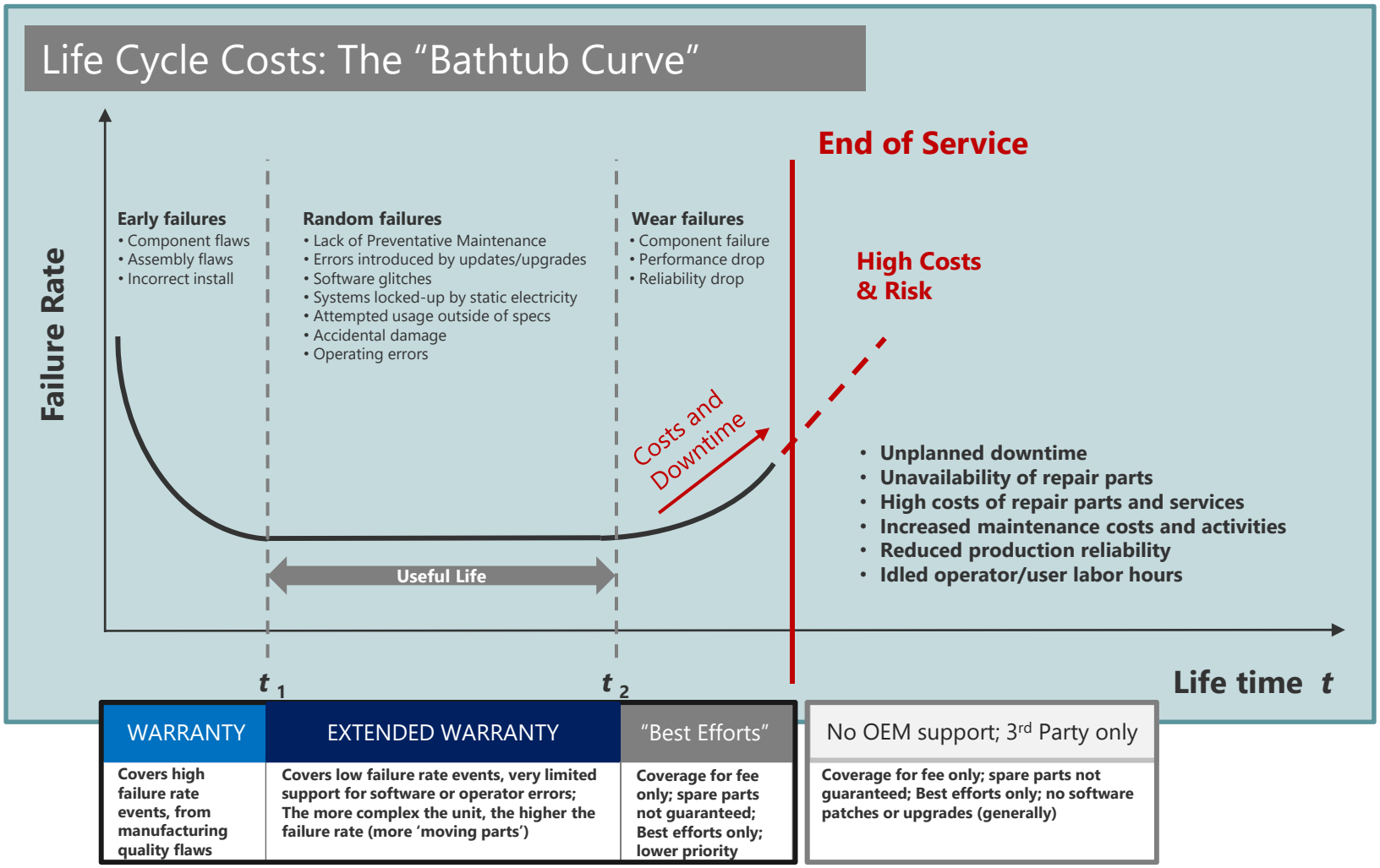
# Executive Summary

- All types of equipment are subject to obsolescence costs, and typically follow the "Bathtub Curve".
- Because the tail end of the Bathtub Curve incurs excessive costs, failures, and business impact, manufacturers' warranty and extended warranties do not cover that period (for the same reason devices should be replaced before then).
- For example, automobiles show a continually rising cost as a car ages.
- End-user devices (e.g. PC's and laptops) reveal an even HIGHER ramp of obsolescence costs, due to complexity of components, software, and user skill levels.
- The cost to maintain obsolete systems is getting WORSE not BETTER.
- Almost all of these TCO costs hit your business P&L, and do not impact central SCM at all.
- The costs of running an endpoint can be estimated for each year after the warranty period it is kept in service.
- **For 5,000 endpoints kept for 5 years, the excess cost to keep those running is $4.8M – OVER what it costs for the first 3 years**.
- SCM has no incentive to shorten the lifecycle, and often does NOT consult TCO data in setting refresh policy
- We recommend this be discussed with SCM, with materials and assistance from Huntington Technology Finance.

# All Types of Equipment are subject to the “Bathtub Curve”

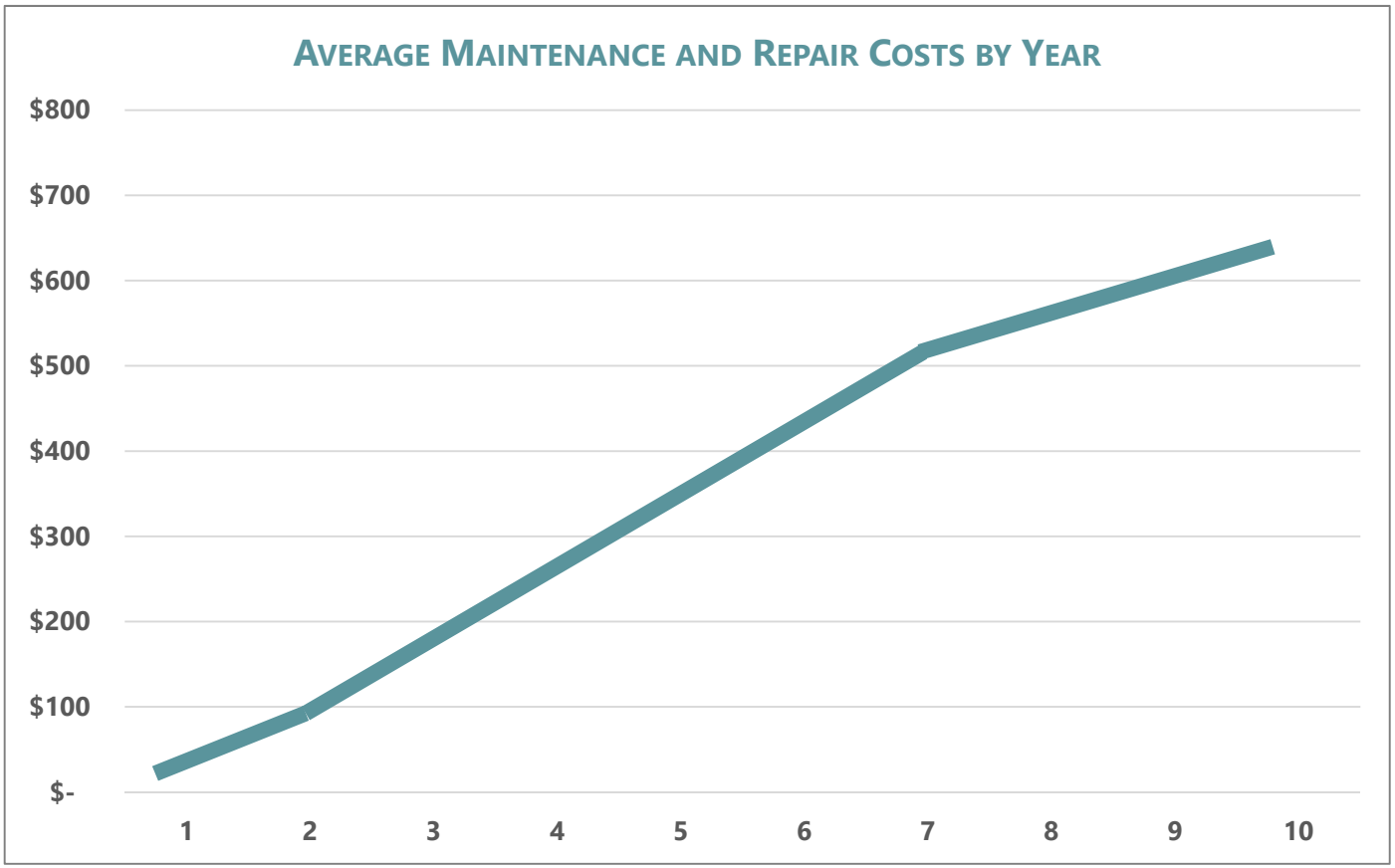


# Manufacturers Only Cover the "Cost-Reasonable" Periods



# Automobile Example

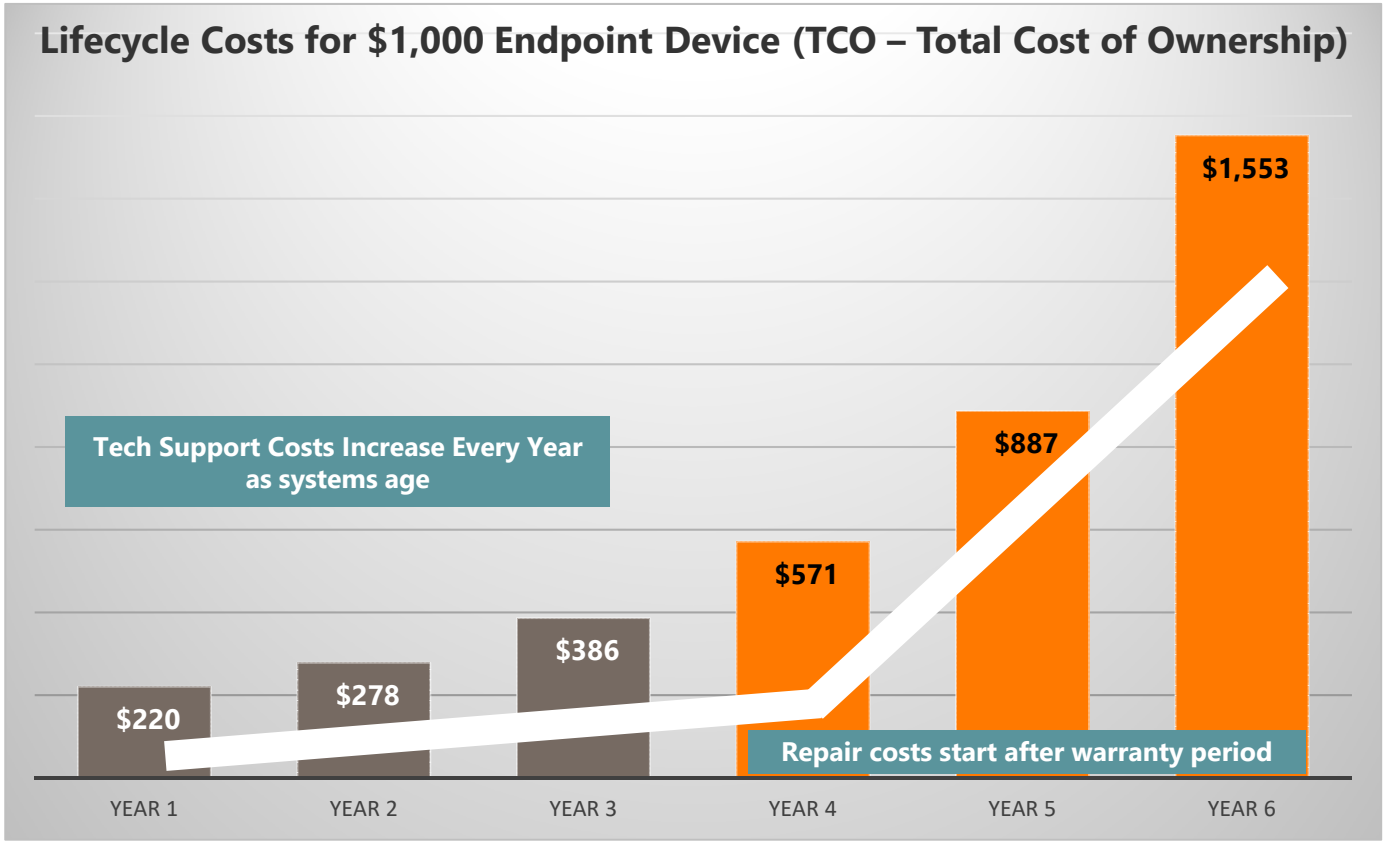
## Overall Yearly Costs Rise by Age of automobile




*Example taken from ConsumerReports (2015), for consumer automobiles

# End-User Devices have much higher obsolescence costs

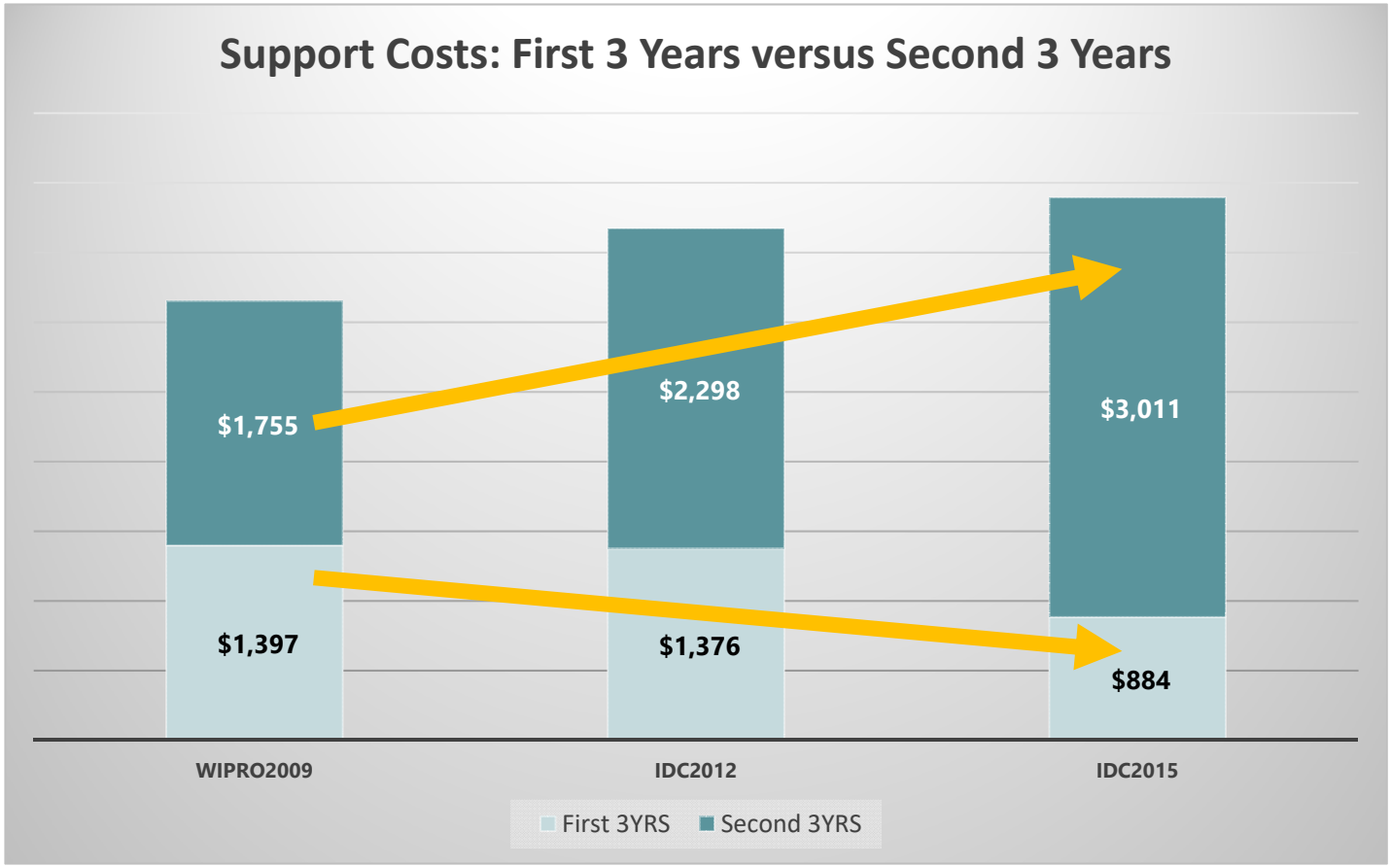
**Post-warranty costs are more "hockey-stick" in shape**




*Source: IDC

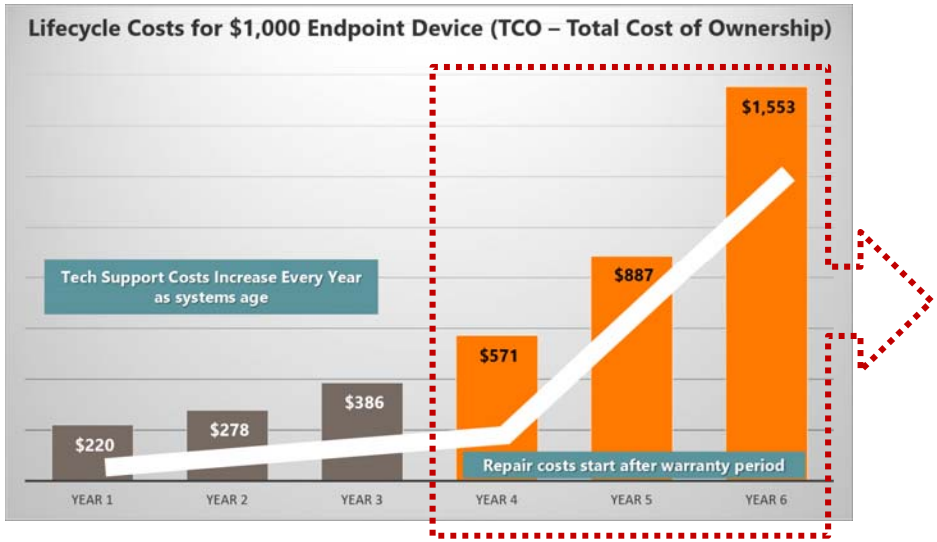
# Obsolescence costs are getting worse for Endpoints

**TCO studies suggest that support for in-warranty endpoints has gotten LESS expensive in recent years, while support for out-of-warranty endpoints has gotten MORE so**



# These Costs are Operating Expenses on YOUR P&L

**Technical support, Repair services, Upgrade Services, Logistics and Administration**




**These TCO costs are being absorbed <u>somewhere</u> in the organization, and typically show up as:**

- Invoices for replacement parts
- Post-warranty repair services or labor
- Extra contract labor in the support team
- Support resources consumed by aged systems
- Upgrades to older systems to keep them in-step with current applications
- Extra infrastructure resources needed for remediation of malware, network, and shared storage problems
- Extra developer resources for application incompatibilities
- Manual labor required for software asset management and audit compliance

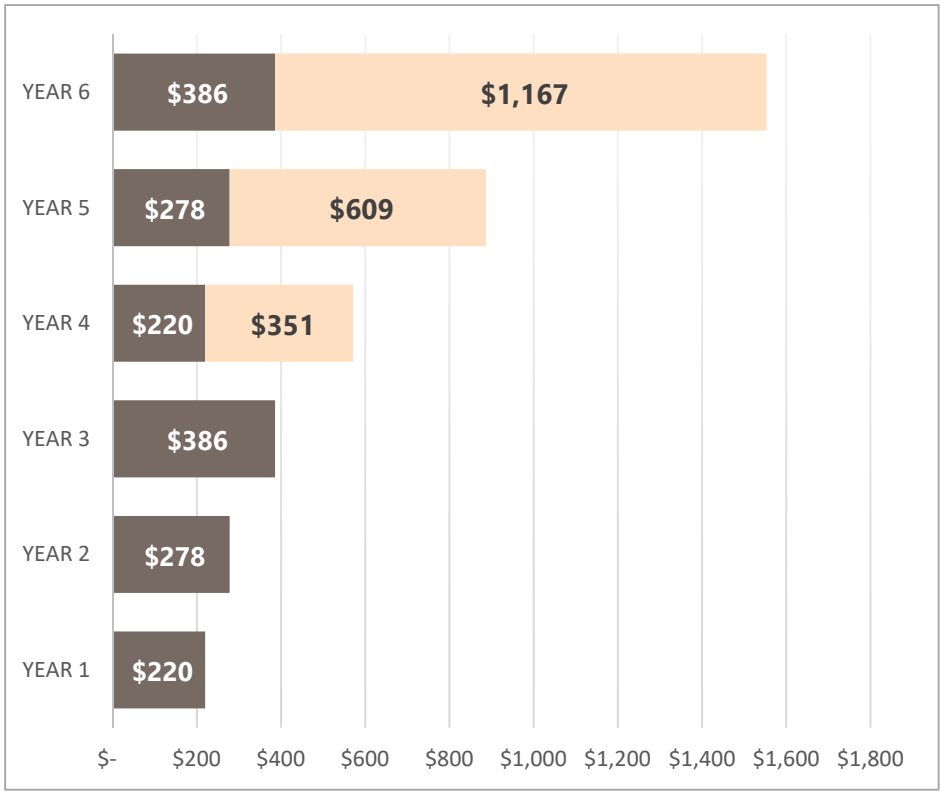
# If Policy/SCM requires users to keep a PC for 4-6 years

**Being forced to keep a PC/laptop running past 3 years COSTS your business P&L*:**

**$351** extra for a fourth year
**$609** extra for a fifth year
**$1,167** extra for a sixth year

**Or**

**$351** extra for a 4 year cycle
**$960** extra for a 5 year cycle
**$2,127** extra for a 6 year cycle




*** In Payroll costs, invoices for parts/upgrades, and contract labor fees or outsourcing fees**

# If Policy/SCM requires users to keep a PC for 4-6 years

**Example: 5,000 Endpoints kept for 5 years**

**$960 extra for a 5 year cycle**

**Multiplied by**

**5,000 PC/endpoints**

**Equals extra displaceable costs of**

**$4.8M***

*** These would be classified as 'waste' under Lean manufacturing definitions**

# If Policy/SCM does NOT factor TCO costs into their policy

**Their supply chain metrics might look good, but they are unintentionally forcing a huge amount of extra operating expense costs onto YOUR P&L.**

| Central Services Supply Chain Mgt (internal or external) | | Your Business P&L |
|---|---|---|
| **Reduces** acquisition costs by delaying replacement of out-of-warranty units, based on accounting useful life. | → | **Increases** operating costs by requiring additional and escalated expenses to support older gear (payroll checks, invoices, service fees). |

# Policy/SCM SHOULD factor TCO costs into their policy

**SCM may have to process more refresh transactions (but fewer *ad hoc* 'spot' orders for repair parts), but this will eliminate a huge amount of extra operating costs from YOUR P&L.**

| Central Services Supply Chain Mgt (internal or external) | Your Business P&L |
| --- | --- |
| **Reduces** OVERALL costs by aligning refresh cycle policy with TCO data; Also eliminates spot orders for repair parts. | **Reduces** operating costs by eliminating waste and high costs to support older gear, and frees up skilled labor for redeployment or reduction in force. |

**Best Practice is for SCM to factor TCO costs into refresh cycle determinations, and to do so by asset classes and/or manufacturer's warranty periods.**

# Recommendation

- **Review the additional materials from Huntington Technology Finance.***
- **Request information from SCM as to**
  1. **What the refresh cycle/lifespan periods for IT equipment are set at;**
  2. **How these lifespans are determined;**
  3. **How TCO studies/data are used in determining those lifespans**

- **If the answer to number 1 is "three years or less", then this process is finished and you can then discuss with Finance what financing vehicles will provide the best economic value and the most favorable impact on the financial statements.**
- **If the answer to number 1 is "more than 3 years", and if TCO is NOT used in determining that lifespan, you should ask the 'Why not?' question.**

- **If their answer to the 'Why not?' question is inadequate to justify YOU bearing all those excess costs, then you should pursue:**
  1. **Setting up an exception process with them (to allow for the correct refresh) or;**
  2. **Developing your own sourcing/SCM capability for <u>this specific class</u> of assets (to cut those costs out of your P&L).**

* Additional Materials:

• DATAPOINTS: "End-User Endpoints" (1 slide);
"2 Endpoints for the Price of 1" (2 slides)

• WHITE PAPERS: "Endpoint Refresh Cycles 2009-2016",
"The Rationale and Economics of Endpoint Technology Refresh in Enterprise"
"Revisiting the Useful Life Factor in Technology Equipment Planning"