



2015 State Of The Industry:

Industrial Equipment

Executives in the industrial equipment sector face many critical and strategic questions in 2015. Here, L.E.K. Consulting shares its views on the state of the industry, including key challenges and opportunities for industrial equipment companies.



What Is the Current State of the U.S. Industrial Equipment Industry?

With the U.S. industrial equipment industry in a state of flux, multiple market forces and shifting business landscapes are keeping senior executives on their toes. For some end-market companies, margins are under pressure from falling commodity prices, yet these same price declines are a windfall for downstream consumers. Regulatory activity is also on the rise, with an increasing focus on air and water quality, which is creating both new opportunities and challenges for industrial players. Furthermore, the revolution in networking and connectivity is ushering in the Industrial Internet of Things (IIoT), expanding the playing field to new areas for growth and competitiveness, and exposing potentially critical gaps in the capabilities of industrial equipment companies. Meanwhile, competitors are growing aggressively through M&A, spinning off non-core businesses to better serve their core markets, and extending into new parts of the value chain as the profit pools shift in response to market trends and forces.



What Are the Key Challenges and Opportunities?

The commercial and operational dynamics of U.S. industrial companies are also shifting. Market players are trying to envision the future of the industry and figure out how their companies can best evolve to benefit from new opportunities while mitigating the downside risks. Most of L.E.K.'s clients observe and experience that the industry has recovered and that growth once again is the key strategic imperative. With that said, industrial equipment companies should look out for a few challenges that they can turn into opportunities:

- 1) Transition from a product and engineering focus to a market and customer focus.** To what extent does your organization understand the channel's and the end user's pain points and unmet needs? Does your company have a robust market and customer intelligence program? How can you anticipate the market's needs and proactively address them, either through product development, customer service, geographic presence, or new capabilities and technologies? How can you serve these particular needs? Doing so will help you win business in 2015. This challenge is not just a question of changes in products and innovation or in sales and marketing; it requires a cultural, strategic change for organizations, and it needs to happen without disrupting existing customer or channel relationships.
- 2) Volatility in energy prices.** Depending on whether you are an energy user or an energy provider, fluctuating prices could present either a challenge or an opportunity. This should trigger strategic discussion on how best to weather the downturn or take advantage of the windfall. Although analysts do not expect further decreases in oil or natural gas prices substantial enough to reduce production activity in the short to medium term, future energy prices may see higher volatility as uncompleted wells and oil rigs are brought back online quickly in response to rising price signals. Developing a strategy to mitigate the impact of energy volatility — or better yet, to thrive in an uncertain energy pricing environment — can set up a company for success.

- 3) Regulation of air quality, water quality and greenhouse gas.** The U.S. Environmental Protection Agency is working on more than 100 proposed new standards and updates to existing standards, many of which touch upon air, water and carbon emitted by industrial users. This evolving regulatory landscape will open up opportunities for industrial OEMs and service providers to help customers meet increasingly stringent standards. For example, the intensifying spotlight on regulation of wastewater and air pollution that result from oil and gas drilling operations has energy executives thinking long and hard about capital investments and new operating procedures to minimize environmental impact. Scenarios such as these can bring opportunities to assist industrial operators in meeting these new regulatory requirements.
- 4) The Industrial Internet of Things.** The IIoT promises to revolutionize industrial processes and operations. The future vision is of networked machines with embedded sensors; advanced analytical tools; and innovative apps to enable novel ways of monitoring, operating and controlling the industrial world. Imagine process manufacturing equipment such as pumps or compressors that self-monitor their mechanical health and send an alarm to the facility manager for proactive maintenance. Or cranes and forklifts in distribution centers that monitor the location of other equipment and personnel, thereby avoiding costly and dangerous collisions. While there is quite a bit of hype and excitement, there is no shortage of uncertainty as well... it is still early days, with most industrial companies having more questions than answers about how to best take advantage of potential technological advances. It will take time to fully realize this vision of the IIoT. Regardless, look for far-sighted industrial companies to begin developing ecosystems of technology partners through joint ventures, strategic partnerships and M&A in order to eventually have a “technology stack” of machines, connectivity, analytics and applications.
- 5) Expanding the service offering.** Whether driven by increasing pressure on profit margins; the desire to further monetize the installed customer base; the need to differentiate in a crowded, competitive field; or the imperative to dampen sales cyclicalities, industrial equipment companies are increasingly developing MRO (maintenance, repair and operations) service capabilities. Service provisioning can increase customer stickiness and provide recurring, highly profitable revenue streams. Be on the lookout in 2015 for more industrial companies to shift their focus downstream to the aftermarket opportunity.



What Burning Issues Are Senior Executives Facing?

In light of these opportunities and challenges to the industrial sector, senior executives are pressured to maintain relevance and push their company's value proposition. Here are several questions to consider:

- How well do you know your customers and the markets they serve? Does your “customer intelligence” function provide strategic insights into your commercial and product development teams?
- How exposed are you to the investment cycle? How can you diminish the cyclicalities?
- Can diversification — either vertically along the value chain or horizontally into adjacent markets — accelerate growth and improve margins?
- How healthy is your innovation engine? Do you have the right people, processes and organization to develop truly transformative products and services?
- Is your organization ripe for change? Are you prepared to enable any of the above transformations?

Our Industrial Products Practice

L.E.K. has developed a deep understanding of the commercial and operational dynamics of industrial companies. Our expertise spans the sector's value chain, including sourcing, manufacturing, product development, sales and distribution. We combine our industry knowledge with a rigorous analytical approach to provide senior executives the strategic guidance they need to achieve genuine competitive advantage.

Meet Our Leaders



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