

## Case 3-1

# Iowa Elevators

Scott McBride, director of purchasing at Iowa Elevators, was reviewing information collected by his analyst, Cathy Ritchie, as he prepared for a meeting with the executive management team scheduled for Wednesday, June 11. Scott had been asked by Walter Lettridge, Iowa Elevator's CEO, to present a five-year plan for the purchasing department at the meeting. In preparation for the meeting, Scott asked Cathy to prepare a report analyzing all expenditures made by the company with outside suppliers over the previous year. It was now June 3, and Scott knew there was still a lot of work that had to be completed to get ready for the meeting the following week.

## IOWA ELEVATORS

Iowa Elevators was one of the largest grain-handling companies in the United States. Headquartered in Des Moines, Iowa, the company had annual revenues of \$2.3 billion

and employed more than 2,500 people. Its two business units were the grain-handling and marketing division and the farm supplies division.

The grain-handling and marketing division operated approximately 300 grain elevators in the Midwest. This division represented approximately 75 percent of total company revenues, although total revenues had declined by 20 percent from the previous year due to drought conditions that had affected farm crop production. Over the previous five years, the company had invested heavily in upgrading its elevator system to improve throughput and increase capacity in key regions.

The farm supplies division sold crop-protection products, equipment and supplies, fertilizer, and seed through its network of country elevators and approximately 30 marketing centers. Revenues for this division had doubled over the previous five years as part of a strategy to tap the company's country elevator network to diversify its revenue base.

Iowa Elevators had a past reputation for steady financial performance and profitability. However, the company had seen a steady decline in profitability over the previous three years. In the most recent fiscal year, it experienced a loss of \$11 million after taxes and a sharp decline in working capital. Management attributed its disappointing results to lower volumes in its grain-handling and marketing division and increased competition. Despite its rising market share, operating margins at the farm supplies division had remained flat.

Concern over the financial performance of the company led to a decision by the board of directors to make changes to the executive team. In February, Walter Lettridge, a veteran of the grain-handling industry, was brought in as the new president and CEO. Shortly afterward, Jose Sousa joined Iowa Elevators as the new chief financial officer. Both Walter and Jose had worked together at a competitor of Iowa Elevators.

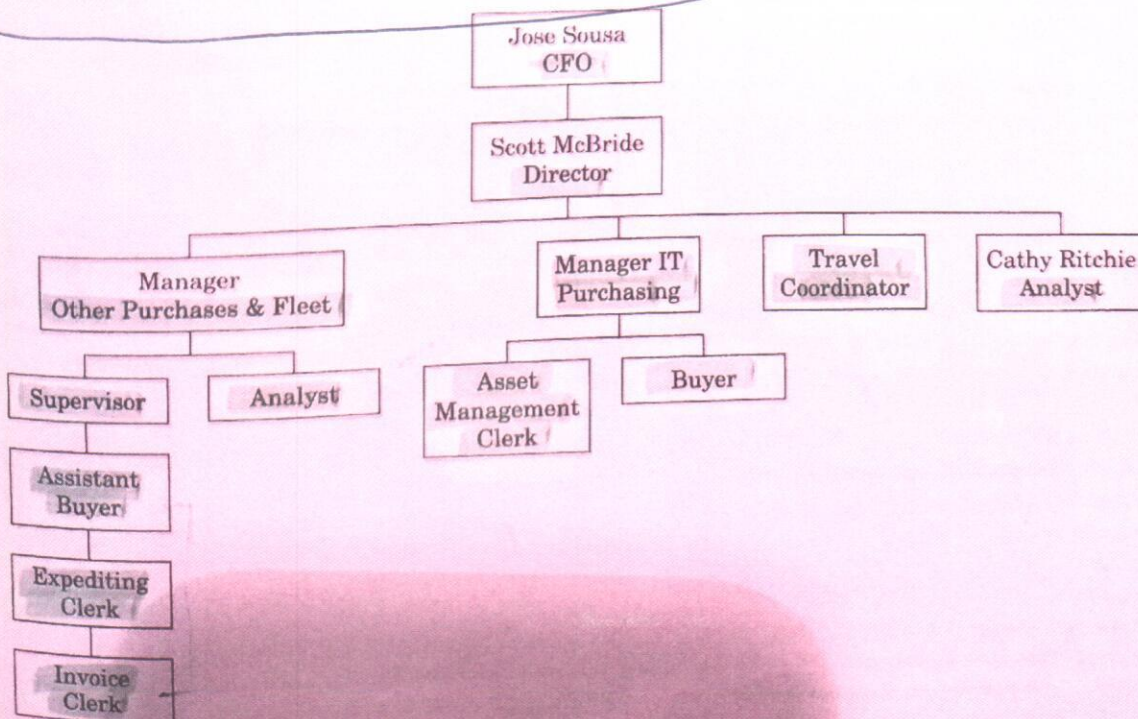
Immediately after joining the company, Walter went to work creating a major cost-cutting initiative, which would include reductions in headcounts, capital expenditure budgets, and overhead expenses. As part of this process, Scott McBride was asked to present a five-year plan to the executive management team, including annual cost reduction targets.

## PURCHASING AND SUPPLY MANAGEMENT

Scott supervised a group of 11 people (see Exhibit 1) who were responsible for the acquisition of requirements for head office and some regional sales and administrative offices. Its major purchases were information technology (hardware and software); printing for forms, brochures, and advertising; office supplies; and company automobile leases. The only change in the purchasing organization within the last year had been the addition of a travel coordinator as a result of a contract for air travel and car rentals. The purchasing organization was part of the corporate services organization, which also included the human resources and information technology groups, and reported to the CFO.

Iowa Elevators had a history of decentralized management, with individual divisions held accountable for their own operations and bottom-line performance. As a result, local elevator managers acted autonomously but were responsible for local market share and profitability. In addition, the elevator managers also made decisions concerning the amount and variety of crop-protection products, fertilizer, and seed stock to handle in their retail

**EXHIBIT 1** Iowa Elevators Purchasing Department



operation. Purchases for elevator operations were handled locally and monitored based on spending limits set in annual operating budgets.

The farm supplies division had a group of four product managers who were responsible for the three main product segments (crop-protection products, equipment and supplies, and fertilizer and seed). These individuals were responsible for supplier selection, product mix, branding, and promotion and assisted elevator and marketing center managers in the areas of promotion, new product development, and inventory planning.

## ANALYSIS OF CORPORATE SPEND

In a meeting in early May, Scott was asked by Walter Lettridge and Jose Sousa to present his five-year plan for the purchasing department at an executive management team meeting on June 11. Walter had scheduled time for a number of senior managers to present their plans and ideas aimed at returning the company to profitability. During the meeting, Walter commented to Scott: "I expect purchasing to deliver cost savings and your group needs to play a more significant role in the company. You need to explain what you can deliver and explain how you intend to accomplish your objectives. As far as I am concerned,

everything is on the table right now. We need to return the company to profitability and I am not afraid to make some major changes in terms of how we run this business."

Recognizing the need to present a thorough plan, Scott enlisted the support of his analyst, Cathy Ritchie, to help him collect and organize data. The data collection focused on two questions: (1) How much money did Iowa Elevators spend with its outside suppliers? and (2) How much inventory did the company carry? The data collection process had been complicated by the variety of management systems at different levels and at different locations. Scott believed that, if more time had been available, Cathy might have been able to capture more spend and inventory data.

Cathy's analysis identified a total corporate spend of \$728 million. Although the company dealt with more than 1,500 suppliers, 20 suppliers accounted for approximately 45 percent of the total spend and the top five represented 35 percent. (The top five suppliers consisted of two railway companies and three suppliers to the farm supplies division for crop protection and fertilizer.) She estimated that average annual inventories in the farm supplies division were nearly \$120 million with annual purchases of \$310 million. A summary of Cathy's key findings is reported in Exhibits 2 and 3.

**EXHIBIT 2**  
Total  
Purchases by  
Category  
(\$000)

| Spend Category                                                 | Annual Spend*    |
|----------------------------------------------------------------|------------------|
| Farm supplies <i>3 farm suppliers</i>                          | \$ 254,406 = 35% |
| Information technology and telecommunications <i>2 railway</i> | 17,187           |
| Fees, levies, memberships                                      | 26,301           |
| Energy                                                         | 8,602            |
| Financial services and interest expense                        | 24,461           |
| Fleet                                                          | 4,229            |
| Insurance                                                      | 5,239            |
| Packaging                                                      | 10,551           |
| Professional services                                          | 7,708            |
| MRO & construction                                             | 127,829          |
| Transportation services                                        | 208,927          |
| Travel and entertainment                                       | 3,557            |
| Other                                                          | 17,350           |
| Miscellaneous and unclassified                                 | 11,926           |
| Total                                                          | \$ 728,273       |

\* Data for the most recent fiscal year.

**EXHIBIT 3****Farm Supplies**

**Division**  
**Inventory**  
**(\$000)**

| Category                 | Average Inventory | Annual Purchases |
|--------------------------|-------------------|------------------|
| Crop protection products | \$ 65,098         | \$ 124,696 < 2   |
| Equipment and supplies   | 22,388            | 13,743           |
| Fertilizer               | 20,938 ✓          | 130,557 6.5x     |
| Seed                     | 10,389 ✓          | 41,787 4x        |
| Total                    | \$ 118,813        | \$ 310,783 2.6   |

*Seasoned and  
 Vendors*

**THE MIS PROPOSAL**

Scott was aware that the MIS Group had been asked to make a similar presentation to the executive management team. The MIS director had informed Scott that he would be requesting \$10 million in additional spending beyond standard upgrades over the next five years with anticipated cost savings of about \$500,000 per year.

**PREPARATION FOR THE MEETING**

Scott viewed the upcoming meeting as an opportunity to redefine the role of purchasing at Iowa Elevators. His session with executive management was expected to last approximately 90 minutes, and he wanted to prepare a five-year plan with specific objectives for each year, including cost reduction targets. In particular, his plan for the coming year had to be very specific and include

identifiable projects and initiatives, schedules, project plans, and expected costs and benefits.

As part of his proposal, Scott also wanted to establish a budget and human resource requirements that would be needed to support his recommendations. While he regarded his staff as competent, Scott recognized that he would require new managerial resources if the role of corporate purchasing was to be expanded. Consequently, he also planned on proposing a new organization structure and establishing a headcount plan and budget for the purchasing department.

As Scott reviewed Cathy's report, he began considering where he was going to start and what could be accomplished. His major concern would be resistance from the divisions and field elevator managers, and he wondered what, if anything, could be done to address any organizational resistance to his recommendations.