

DELTA STEEL COMPANY

The Delta Steel Company produces a large annual tonnage of sheet steel, tin plate, galvanized sheets, black plate, merchant bar, and other products. Company operations are on a substantial scale, as indicated by the fact that annual purchases, exclusive of capital equipment, average \$200 million.

Supply management is centralized in a department headed by the director of supply management, who reports directly to the president of the company. The director of supply management is, therefore, on a coordinate organizational level with the executives in charge, respectively, of operations, engineering, marketing, and finance. The supply management department personnel consist of the director, the assistant director, supply managers, clerks, and typists. The director, in addition to his responsibility for general administration of the supply management function, formulates supply management policies, handles the major problems of coordination with various departments of the company, and represents his company in those industrial, governmental, and other external activities involving important procurement matters. Although thousands of different items are bought during the course of a year, the director concerns himself with the purchase of such principal items as major capital equipment, construction, and raw materials, including those requiring contract negotiation, such as steel scrap and sulphuric acid.

It was the supply management department's normal practice to have several sources of supply for all-important materials and continuously to seek new and better sources. For the past fourteen years, however, the Delta Steel Company had contracted for its entire requirements of sulphuric acid from the Eureka Chemical Corporation, a subsidiary, of a large metal mining and smelting company. Because of the fact that the Eureka Chemical Corporation produced sulphuric acid as a by-product from smelter stack fumes, its costs were appreciably less than the costs of several local chemical companies that manufactured the acid from natural sulphur. In fact, the price of locally produced sulphuric acid was from 15 to 20 percent higher than the delivered price of the Eureka Chemical Corporation, although its plant was several hundred miles distant. Delta did purchase excess requirements from either of two local suppliers on occasion.

Despite the price disadvantage that they faced, the local chemical companies had regularly and aggressively solicited the sulphuric acid business of the Delta Steel Company. They pointed out the hazards of a single source of supply and the propriety of patronizing local industry. Sulphuric acid is not only a critical item in the manufacture of certain steel products, but one involving considerable annual expenditure. In the case of the Delta Steel Company, purchases of this acid amounted to \$1.7 million or more in a year of capacity operation.

Sulphuric acid is used for the pickling of strip steel after the steel has been hot rolled. The long strips of steel are passed through a 25 percent solution of acid, which removes scale, oil, grease, and dirt. This surface cleansing is essential before tin plate or galvanized sheets can be made, since otherwise tin or zinc would not adhere properly to the steel. Even for steel sold in the form of black or uncoated sheets, the surface must be similarly pickled before the subsequent operation of cold rolling. For pickling purposes, only the highest grade of sulphuric acid is usable. In "trade terms," this grade is specified as pure virgin acid or 100 percent H₂SO₄.

Sulphuric acid is essential to the manufacture of a wide variety of products other than steel. Among them are gasoline, paper, fertilizer, and chemical products ranging from rayon to explosives, dyes, rubber, and paint.

During a current period of scarcity of sulphuric acid, the plant of the Eureka Chemical Corporation was closed down by a strike. The Delta Steel Company had experienced no short-age, however, as the Eureka Chemical Company, in order to fulfill its contract obligations, had purchased sulphuric acid from the local manufacturers and absorbed the difference in price.

As the strike extended well into the second month, the vice president of operations of the Delta Steel Company became increasingly concerned over the situation. He voiced anxiety as to whether there would be an interruption in the shipments of acid. Steel companies do not store large quantities of sulphuric acid, depending instead on scheduled daily receipts.

The director of purchases stated that he had implicit confidence in the Eureka Chemical Corporation's management and that, in accordance with the terms of the contract, three tank cars of acid had been received at the steel mill daily. Moreover, he said that the contract contained a cancellation clause that permitted either party to withdraw from the agreement on ninety days' notice and, as yet, the supplier had not availed itself of this privilege. The vice president of operations still had some misgivings. He argued that the strike could well be a protracted one, and the Eureka Chemical Corporation could properly exercise the ninety-day cancellation provision. At the end of that period, the Delta Steel Company would have to rely on local suppliers. The present scarcity of acid, together with the vulnerable position of the company, might well mean a substantial increase in the price of acid, with a resultant increase in steel production costs.

The director of purchases took the position that his company had benefited financially and in other ways from its long and satisfactory relationship with the Eureka Chemical Corporation. He did not feel, after fourteen years, that such a relationship should be abandoned when that particular supplier had the misfortune to be shut down by a strike that might be settled at any time. He also pointed out that any purchasing transaction is a two-way proposition and should be mutually advantageous to buyer and seller. He stated that trade relationships developed on this basis are invaluable, and related the instance in which he had voluntarily testified in a freight-rate case on behalf of the Eureka Chemical Corporation a year or so ago. The local manufacturers of sulphuric acid had petitioned the Interstate Commerce Commission for an increase in freight rates on acid into the local territory. If the increase had been granted, the delivered price of sulphuric acid for the Eureka Chemical Corporation to the plant of the Delta Steel Company would have been 10 percent more than that of the local manufacturers. This would undoubtedly have precluded the Eureka Chemical Corporation from participation in the local business. Finally, the director of purchases expressed confidence in being able to negotiate a contract with either or both of the local suppliers in the event that the Eureka Chemical Corporation terminated its contract.

The vice president of operations remained unconvinced and continued to question the practice of concentrating the purchases of a vital commodity with a single supplier—a commodity, furthermore, for which there was no substitute. In his judgment, there was a long but indefinite period of capacity operations ahead, and every means practicable should be taken to prevent any interruption to production. He suggested that in view of their opposed opinions, he and the director of supply management take the matter before the president of the company.

1. If you were the president of the Delta Steel Company, what decision would you make regarding this controversy? Explain why.
2. With respect to sulphuric acid or any other item of major importance, what are the advantages and the disadvantages of concentrating purchases with a single supplier?
3. What are your reactions to the proposition of patronizing home industries as advanced by the sales representatives of the local acid manufacturers?
4. The director of supply management in the Delta Steel Company reported to the president. Under what circumstances do you think the supply management function should enjoy equal organizational status with such other functions as engineering, production, marketing, and finance?