

# Armco. case

Business



Armco, Inc. (Armco) is the sixth largest producer of stainless, electrical, and carbon steels and steel products. Kansas City Works (Kansas) is the Armco's Midwestern Steel Division, and has two primary products: grinding media and carbon wire rod, one being recognized in the industry for its durability while the latter being non profitable and only covering some of its fixed costs through volume. In January 1991, Bob Nenni, the Director of Finance, introduced a new performance measurement system for Kansas City Works to provide managers with the best information that would better enable them to boost up company performance.

In order to maximize profits and sustain its position in the US manufacturing steel industry, Armco has adopted a cost leadership strategy with a broad appeal and has managed to achieve growth by engaging in joint ventures expanding its product lines in implementing its strategy.

However, the Kansas City Works has the strategy based on differentiation because it has cost disadvantages such as inefficient plant infrastructure and union labor costs.

Taking into consideration that Armco's revenue has been declining and now only generates a marginal profit whereas Kansas succeeds in producing and selling high value products, Armco as a whole should switch the strategy to focus on the differentiation strategy that will lead to sustainable growth and leading position in the industry. In addition to this inconsistency with the strategies of the firm as a whole, the old management control system used at Kansas had numerous problems that lower the quality of performance measurement.

In the old system, the Operating Statics Reports were issued only monthly and provided to the managers approximately 15 days after the following month. The lack of timeliness caused manufacturing results measurement controls to be ineffective because variances could not be investigated quickly. This also caused delay in solving problems and contributed to higher manufacturing expenses in the following month's financial statements.

Also, the old report contained too detailed information and issued that managers do not have control over.

It included the same accounting information that was used for other purpose. As a result the numbers included allocations of indirect manufacturing costs. The too detailed information caused distraction from focusing on important issues to less important and less relevant issues. Another problem with the old system was that it failed to measure performance of managers and employees at different levels because of the subjectivity and basis that is not applicable to all employees.

Therefore, the old system did not serve as a good results control system due to the inefficiency.

Due to the aforementioned problems, a new performance measurement system was introduced to replace the old management system. It was designed to give better management focus on the things, which are most important. The new system included less data's: it allows managers to focus on the 5-6 more important which cause 80% of the costs. Furthermore, the new system has more balanced set of performance measures, which

provides an improved basis for evaluating operating managers and manufacturing supervisors.

The design of the new system was more sophisticated than the old one; however, the top management failed to smoothly implement the new system.

First, the managers have been working with the old system for a very long time and they are more familiar using the old system. Secondly, the old system suffers from lack of direction as employees did not fully appreciate the relationship between their responsibility and their final results.

Due to the lack of explanation to employees, managers kept using the old performance measurement system because they were accustomed and they didn't know the differences between the two systems, so they never seriously considered improvements that could be made with the new. Therefore, there was a miscommunication between the top management and the middle and lower managers. The lack of information they get leads to poor understanding of the use of the new system and a lack of motivation of middle/lower managers to use it.

In conclusion, as managers complained, " It almost seems like the operating managers finally understood the old report, so they decided change it", managers did not understand the purpose of writing reports and recognize the importance of specific information in the reports. Thus, more communication was needed to explain the goals and needs of the new system so that middle and lower managers can fully understand expectations for them and take advantage of the new system to improve

efficiency. Better communication between management will be achieved by having seminars and meetings where they can have opportunities to share opinions.