

Case study on armco, inc.: midwestern steel division

[Business](#), [Management](#)



Armco Inc. was the sixth largest steel manufacturer in the United States at the end of 1990 and employed about a thousand employees in its production facilities. Being in a labour and capital intensive and declining industry with low margins meant that managers at Armco had to be very careful with their spending to stay competitive. Part of the plan to stave competition was to produce higher quality goods and raise employee performance with incentives programs based on employee responsibility and historical performance.

The old method of performance evaluation was based on ' Cost Above' system, a plan that summed up the costs that were added on per ton of steel produced in a shop. Managers would receive a comprehensive report that showed monthly, five-year historical and year to date figures for all the costs alongside the variances for each in their shops. These reports were very comprehensive and included all items that generated costs in a shop such as Non-metallic used, repair, maintenance and outage, energy consumptions and salaries amongst other things. Since figures were reported on a ' per ton of steel' produced, figures would often be tiny, fraction of cents.

The new system that was introduced in 1991 brought along several changes in the reporting of performance evaluation. The new reports changed focus from the sum of everything that occurred in a shop to certain key cost contributors that occurred in a shop. Another key improvement that the new system introduced was the inclusion of balanced performance evaluation measures and included safety, schedule achievement and quality, all in addition to costs. All reports and costs would also be reported per individual operator and not by volume of steel produced.

Factors determining the success or failure of Midwestern Steel

The Midwestern Steel Division had been facing a steady decline in production over the last couple of years due to increased competition over the world and comparatively higher cost of productions in the United States. On top of that, the largest contributor to the Division was Kansas City Works, which while operating at a marginal profit, was not a low-cost manufacturer. The labour unions that worked in Kansas City charged higher compared to other manufacturers in the US. Also, due to the reduction in workforce and demand, the plant was not operating at peak cost efficiency as it was laid out to accommodate a much larger workforce.

The Kansas City Works attempts to maintain success by producing higher quality goods compared to their competitors. Where this was impossible to achieve due to older machinery and plant layout, they kept costs low by producing larger volumes. This just highlights the importance of costs in the manufacture of steel across the US, as profit margins are very low.

Old System Performance, Strengths, and Weaknesses

The old system of performance evaluation worked by reporting all costs that a shop incurred on a monthly basis. Alongside the monthly statistics, the report also displayed historical five-year data with a year to date figures and variances from historical. All figures were cost-based, calculated on the cost that each shop added on each ton of steel produced. These costs were broken down into several categories including shop specifics and general categories, eventually summarizing all costs involved in the shop. This presented managers and supervisors with all the data that they might need

in eliminating extra costs while monitoring all the changes that occurred in the past month.

Since all values in a shop were reported, managers could keep a strict eye on the running costs involved in the shop. Comparisons of historical trends could be made immediately, and any irregular increase or decrease within a shop would stand out. This helped managers control the performance of their shop.

Problems with the system meant that often, when unorthodox costs came along that didn't fall in any category in the reports; they would get added in the sheet, whilst not really being under the control of the shop managers. Costs per ton of steel produced meant that low volume months would display disproportionately high costs as overheads didn't change. Also, some of the costs would be displayed as fractions of cents compared to others and didn't really make sense being shown. There were also no dedicated aspects that measured employee performance and hence made management a tedious task.

New System, strengths, and Weaknesses

The new system really improved on the performance evaluation aspect of the reporting, creating a several new measure to be displayed that calculated employee performance. This was displayed alongside the costs that were necessary to the running of the shop. Cost that were only necessary to the running of the shop meant that managers weren't inundated with lots of data that would often times not mean anything, allowing them to focus on the costs that matter to the shop and not the trivial costs that had little effect. Costs displayed were now only shown when

they could be directly influenced by the operators themselves and were independent of the volume of steel produced. Better breakdowns of the costs involved as a result of better reporting allowed managers more descriptive data of how their shop was running.

Issues with New system

The new system had some problems that were related to performance evaluation, not related to the display of costs. The evaluation of manager's performance was hard to manage when costs that were not in the control of the company made themselves evident. The decision to add these costs to the reports was something that needed to be considered as the new system ignored them by default. Another issue that the company faced with the new system, it became clearer that employee performance was going to be displayed with more clarity. Hence, a decision had to be made whether to increase compensation or change the ratio of paying incentives to people who performed well at their jobs.