
3 Don't Shoot the Messenger¹

On July 5, 2000, the unit general manager of Billings Equipment, Inc. instructed the supply management team to renegotiate existing agreements for a 10 percent reduction with major suppliers due to target costs exceeding expectations. Jeff Martin, a supply management engineer, was instructed along with the entire purchasing staff to contact his suppliers immediately with what they would view as very bad news. Jeff had to face his suppliers with this demand.

Company Background

In June 1998, Billings Equipment Inc. formed a new business unit and opened a plant in Seattle to produce a new line of earth-moving machines for the construction industry. The organization had a history of impeccable ethical treatment of suppliers and was considered to be a leader in the industry. For two years, Jeff was actively involved in reducing costs and cycle times of his suppliers. Everyone involved would agree the process was emotionally heated on occasion, with shedding of cooperative blood, sweat and tears. Jeff's suppliers had invested many personal hours and sizeable expense to reach this point in time. It had evolved into a strained, but working, relationship.

Relationship with Suppliers

During the start-up period of the program, a very aggressive timeline and target cost drove emotions to a frenzied pace. Early supplier involvement in prototype and testing activity was cultivated to encourage active participation in the development of this new product line by all that had equity in its future. Suppliers were pushed to the limit on material and tooling lead-times, exhausting goodwill and testing commitments. Everyone involved, including suppliers, invested personal time and effort toward meeting the market timelines. Purchase agreements were negotiated, and parts now were being received to support production ramped-up toward market introduction.

The Problem

The push to production forced acceptance of early design of many components, which inhibited additional cost reduction. Customarily, 80 percent of cost reduction occurs during the design phase. Tooling was developed during early design configurations to meet the production schedule. As designs became frozen and cost information became more complete, the projected total costs were going to exceed target levels by as much as 20 percent. As the costs for the bill of materials (BOM) continued to rise above

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target levels, it became clear that this increase was not simply due to procedural or accounting errors, but rather represented true costs. The general manager realized the rising cost situation was beyond recovery and would impact the market pricing and success of the entire product line. At this time, Billings Equipment, Inc. had invested U.S. \$20 million to U.S. \$30 million in sunk costs for the plant and pre-production efforts. Something drastic would have to be done.

The Ethical Issue

In an effort to at least “stop the bleeding,” a letter was sent to suppliers on July 5 declaring the regrettable necessity to reduce prices by 10 percent within 30 days. Buyers were to follow up immediately by contacting their top 30 suppliers. The veiled threat for noncompliance to re-open previously negotiated agreements indicated a possible cancellation of the product line altogether, or at least a consideration of other sources of supply. Jeff believed he would be violating a trusted relationship based on the heroic collaborative effort to meet demands over the past year. How could he carry this message to the suppliers?

Even with some additional eroding of supplier tolerance for concessions, Jeff succeeded within the 30 days to get agreement from four of his five major suppliers, which represented 80 percent of the cost of materials he purchased. About 20 percent of the suppliers complied promptly, within 30 days. Other buyers had mixed results. Everyone was uncomfortable moving the supplier relationships from a cost-based approach to a simple request for price reduction.

Now the Other Shoe Drops

Shortly after the most faithful of the major suppliers reluctantly committed to cutting prices, the general manager made an announcement during a strategy meeting with buyers. “Because some suppliers complied readily with the 10 percent price reduction,” he said, “we are now going to push for an additional 5 percent.” This implied that suppliers had padded prices and further reductions could have been done all along. In effect, the suppliers who had complied with the first request were to be penalized.

Jeff was now faced with an ethical situation pitting his responsibilities to the general manager against carefully developed supplier relationships.

Discussion Questions

1. If you were in Jeff’s position, what would you have done to preserve relationships?
2. Describe the ethical issues involved.
3. What is your assessment of the general manager’s approach to meeting target cost objectives?