



## **FARMCHEM'S DILEMMA: Coping with Distribution Challenges in the Supply Chain Management**

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### **Teaching Note**

#### **1.0 Synopsis of the case**

It was on Monday, the 3rd of April, 2011, when Mr. Charles Mulinge, the Chief Executive Officer (CEO) of Famchem Ltd, a firm dealing in crop disease curative products, received a phone call. "Hallo!" he answered the phone. The caller went on but a look at the CEO's face was not amusing. After about five minutes, he banged the receiver back. "What is it with these middlemen?" he mumbled to himself. The caller was a field officer covering Mount Kenya Region. "Sir is there something wrong?" his secretary enquired. "That was Mount Kenya Regional Manager reporting again that the distributors in his region are not delivering orders to the farmers on time and are overcharging by a margin of 10%, making our products more expensive and therefore not moving". After a long pause, he asked the secretary to invite the Operations, Finance, HR Administration and marketing Managers for an immediate meeting in his office.

"Lady and gentlemen, good morning again" he greeted his management team and continued. "Today we consider and decide whether we should maintain the status quo or shorten our supply chain by selling directly to farmers". The meeting continued.

## **2.0 Learning objectives:**

At the end of the session, the student will be able to:

- a) Define distribution , as defined in the Agribusiness
- b) Explain the importance of distribution in Agribusiness
- c) Explain types of distribution channels
- d) Develop skills to choose efficient /competitive distribution channels

## **3.0 Target Market**

The case is suitable for the Certificate in Management and Innovation for Agribusiness Enterprises, Diploma in Management and Innovation for Agribusiness Enterprises, beginners' course in marketing and Supply Management

## **4.0 Teaching Approach and Strategy**

The case will be issued to the learners one week before the session so as to familiarize themselves with the content of the case. At the class session, the learners will be grouped into small discussion groups to enhance group learning and gain synergy from the group. Thereafter the class will assemble in the plenary session to undertake deep discussion about the decision issues, the alternative taken and the justification. The students will present the pros and cons of the arguments.

The instructor will guide the plenary case discussion without enforcing his/her views on the learners. The instructor will guide the students after analysis of the various options available.

## **5.0 Case issues and underlying problems**

### **5.1 Case decision issue**

The major issue in Farmchem is:

Does the company retain the distributors in its supply chain or does it phase away the distributors and establish stockiest.

### **5.2 Underlying problems or challenges**

- The company is experiencing inordinate delays in the supply of its products to the final consumers
- The distributors are over-charging Farmchems' products by 10%
- The separation of final consumers from the Farmchem results in reduced loyalty. Farmchem is unable to address the problems that the final consumers of their products face due to the barrier created by the distributors
- The products are likely to be adulterated, making them less effective and more harmful to people and environment.

## **6.0 Analysis of Assignment and Discussion questions**

- a) What would you consider to be the business challenges facing Farmchem?
- b) What business triggers have Charles Mulinge's considered?
- c) Summarize the pros and cons of each of the possible distribution option in the case.
- d) Compute the funding required to sustain the distribution chain options
- e) Outline supply/distribution channels available in the case
- f) Compute the financial benefits in each of the supply/distribution options
- g) Develop a criteria of evaluating efficient distribution channels for Agribusiness Enterprises
- h) Explain why Just in case (JIC) and Just in time (JIT) are important considerations in the supply chain management. In your view which approach is being adopted by Farmchem?
- i) Explain why Farmchem may wish to apply Environmentally Preferred Purchase (green purchasing)
- j) Adulteration is a serious problem where the distributors break the bulk. Explain how this may have impacted on Farmchem.

## **6.0 Analysis of Assignment and Discussion questions**

- a) **Farmchem is faced with distribution dilemma** such as the delays in the delivery of the products, overcharging the products by 10%, reduced loyalty and likely adulteration of products.

**b) Charles Mulinge considered the following business triggers:**

- Delays in order deliveries
- Additional charges
- Adulteration

**c) Summary of pros and cons of each of the possible distribution option in the case.**

	<b>pros</b>	<b>cons</b>
<b>distributors</b>	<ul style="list-style-type: none"> <li>-Coverage wide</li> <li>- Already exist structure</li> <li>-Distributed in all coffee and maize growing areas of kenya</li> </ul>	<ul style="list-style-type: none"> <li>-Uncertainty</li> <li>-Adulteration</li> <li>-Absence of training</li> <li>-No loyalty</li> <li>-Unauthorized increase in prices</li> </ul>
Direct through agrovets	<ul style="list-style-type: none"> <li>-Certainty</li> <li>-loyalty</li> <li>- awareness through training</li> </ul>	<ul style="list-style-type: none"> <li>-Heavy investment of ksh 20million</li> <li>-Staff issues</li> </ul>

**d) Required funding to sustain a distribution option**

**Creation of agro-vets ksh**

Establishment cost  $400,000 * 50 = 20,000,000$

Staff costs  $50,000 * 50 * 12 = 30,000,000$

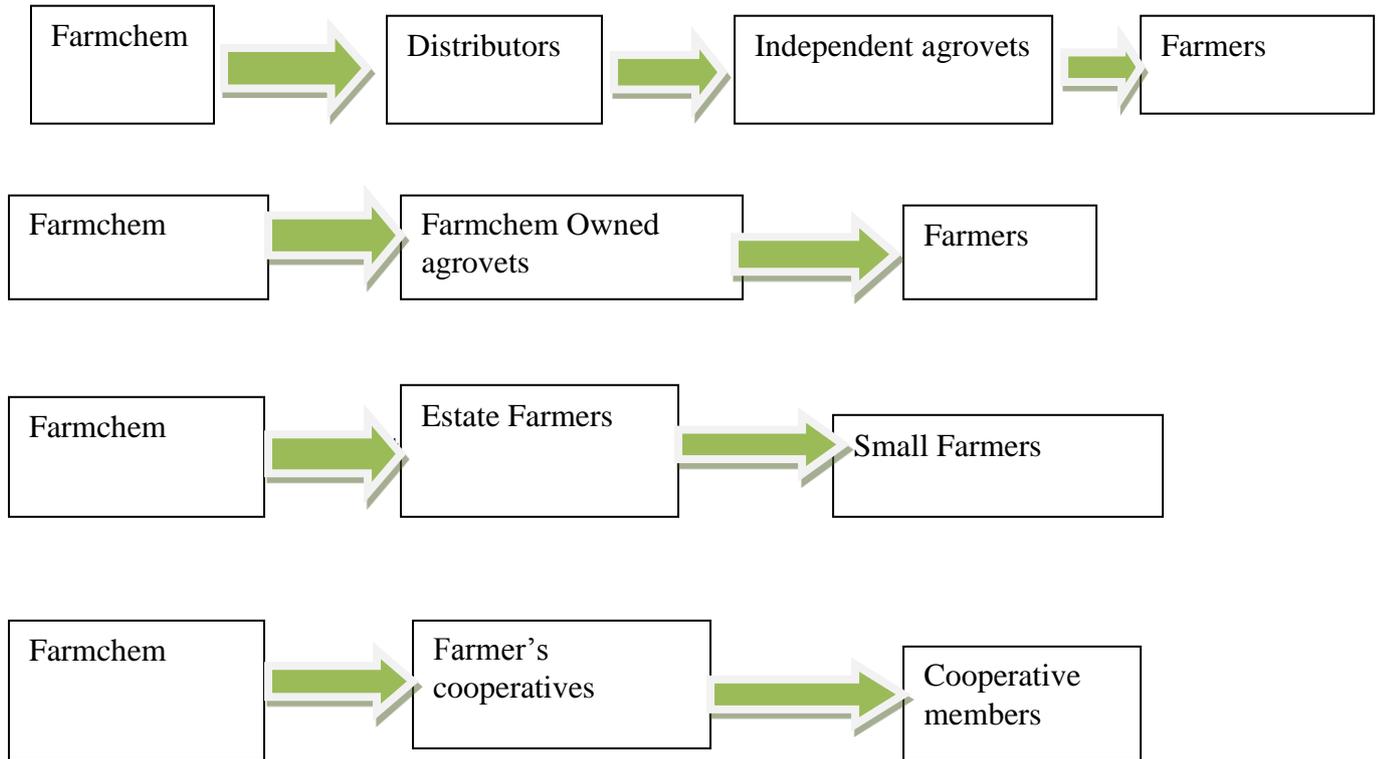
Other overhead costs  $50,000 * 50 * 12 = \underline{30,000,000}$

Total annual cost of creating agrovets  $80,000,000$

**Use of distributors**

Distributor charge  $500,000 * 50 = 25,000,000$

e) The supply/distribution channels available in the case are:



**Agrovet**

Sales  $2,000,000 * 50 * 12 = 1,200,000,000$

Cost of sales  $11,500,000 * 50 * 12 = 920,000,000$

**Gross profit 280,000,000**

Interest on initial funding

$20,000,000 * 20%$  4,000,000

Net gross profit **276,000,**

**0000**

Gross profit per store per annum 5,520,000

Gross profit per store per month **460, 0000**

**Distributors**

Sales volume 10,800,000 \*50 540,000,000

Cost of sales 540,000,000/1.3 415,000,000

Gross profit 125,000,000

Distribution charges 500,000 25,000,000

**Profit before operating expenses 100, 000,000**

**g) The criteria for evaluating efficient distribution channels for Agribusiness Enterprises is as follows;**

<b>Criteria</b>	<b>Evaluation</b>
1.Delivery of products to Customers	
2. Pricing of the Products	
3.Quality of the product ( Handling of the products	
4. Customers support	
5.Terms of business	
6.Mixed of products that compliment	

your products	
7. Market coverage	
8. Operation costs	

g) Just in case (JIC) and Just in time (JIT) are important considerations in the supply chain management because the two concepts deal with inventory management issues which are very important in supply chain.

JIC is an inventory management strategy in which companies keep large inventories on hand. It aims to minimize the probability that a product will sell out of stock. A company practicing this strategy essentially incurs higher inventory holding costs in return for a reduction in the number of sales lost due to sold out inventory.

The JIC inventory strategy is much different than the newer 'just in time' (JIT) strategy where companies try to minimize inventory costs by producing the goods after the orders have come in.

The older 'just in case' strategy is used by companies that have trouble forecasting demand. With this strategy, the companies have enough production material on hand to meet unexpected spikes in demand. Higher storage costs are the main disadvantage of this strategy.

### Comparison between Just in Case and JIT Purchasing

<b>Purchasing Activity</b>	<b>Just In case Purchasing</b>	<b>JIT Purchasing</b>
Establishing lot size	Purchase in large batches with infrequent deliveries	Purchase in small lots with frequent deliveries
Selecting suppliers	Multiple sourcing with short term contracts	Single source for a given part, with a long term contract

Evaluating suppliers	Price, delivery and quality in that order	Product quality, delivery performance and price; (Zero rejection expected)
Negotiating with suppliers	Lowest possible price is the prime objective	Product quality, fair price, long term contract is the prime objective
Incoming inspection	Buyer is responsible for receiving, counting and inspecting all incoming parts	Counting and inspecting of incoming parts is eventually reduced and eliminated
Determining mode of transportation	Concerned only for out bound Freight (of finished goods). Delivery schedule within a month is left to the supplier	Concern for inbound, outbound freight and outbound on- time delivery. Delivery schedule is decided by buyer
Setting product Specifications	Buyer relies more on design specs than on product performance. Suppliers have little freedom in innovation design specifications	Buyer relies more on performance specs than on product design. Supplier is encouraged to be more innovative
Inventory Management	High inventory	Low inventory

**h) Farmchem may wish to apply Environmentally Preferred Purchase**

**(green purchasing) due to the following;**

- To comply with National Environmental Management Authority on waste management
- As part of corporate social responsibility

i) **Adulteration is a serious problem where the distributors break the bulk.**

**Explain how this may have impacted on Farmchem.**

- Dilute the quality of Farmchem products
- Erode farmers trust on Farmchem products
- Reduced sales volume
- Give undue advantage to competitors products

**7.0 Management Model to be applied:**

**Michael Porter's 5 forces**



Figure 1, above demonstrate the challenges inherent in the sale /purchase scenarios. Indeed the suppliers and the customers may have varying degrees of power over suppliers. In the case of Farmchem, the distributors have enormous power over the customers. They dictate terms.

Farmchems products are under serious threats from the substitutes that the distributors stock. The company is further faced with the problem of new entrants in the market place to distribute the crop disease curative products and accessories.

Customers have an upper hand due to bargains and therefore distributors make the choice as to which products and accessories to dispose. Indeed they are guided by larger margins and commissions from the wholesalers or manufacturers.

## 8.0 Readings

- Supply Chain Management, Daniel N Burt, 8<sup>th</sup> Edition, 2010
- Supply Chain Management Strategy, Planning and Operations, Sunil Chopra, 3<sup>rd</sup> Edition, 2010.
- Purchasing and Supply Chain Management ,Kenneth Lysons and Michael Gallingham, Sixth Edition
- Ziggers, G.W. & Trienekens, J. 1999. **Quality Assurance in Food and Agribusiness Supply Chains: Developing Successful Partnerships**, International Journal of Production Economics