Editors

Dr. Vinita Sahay | Dr. P R S Sarma

Handbook of MANAGEMENT CASES

ET CASES

ENABLING DECISIONS

AN INITIATIVE BY

TIMES OF INDIA GROUP

Handbook on

MANAGEMENT CASES

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FOREWORD

The case study method of teaching plays an essential role in management education. The pedagogy today has been adopted by several business schools worldwide. The case method is a form of instructor-guided, discussion-based learning tool where instructors use questions, debate and application of analytical tools and frameworks to engage students in a challenging, interactive learning environment. Case Studies enable students to put themselves in the shoes of actual practitioners and test their understanding of theory, ability to connect theory with application, and develop theoretical (or practical) insight. The participants act as co-creators of the learning process in the case method. In case method of learning, students get to see a real situation in a holistic setting and are required to analyze situations, develop alternatives, choose plans of action and implementation, communicate and defend their findings in small groups in class. Cases are more likely to engage students in the classroom than conventional mode of teaching. However, there are very few cases available on the Indian context, and hence make it sometimes difficult for students to link the Case with their experience. To bridge this gap and to create a repository of India-based cases (or Indian Cases), IIM Raipur organized Global Summit on Management Cases (GSMC) during February 4-6, 2016 in association with ET Cases. This summit received overwhelming response from industry and academia in terms of classic cases in all the areas of management.

We believe that the cases included in this book will be highly beneficial to management students, research scholars, faculty and practitioners in their search for best Indian cases. It will be our future endeavor to contribute more such case collections.

Editors

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MARKETING MANAGEMENT

STG-2-0028

LACK OF OXYGEN

Mikhail V. Plotnikov
Professor at National Research University Higher School of Economics,
Dean at Vadens Business School

January 25th 2007, Nizhny Novgorod, Russia:

It was high time to finish the Board meeting, yet its members couldn't agree which way to lead *Kislorod Group*. Supposed to dot the i's and cross the t's, the voting actually split the Board into two equal uncompromising parties. The first party insisted on the profound development of production capacity and putting special attention to the increase of quality and cost reduction as the only viable way to obtain sustainable competitive advantage. The second voted for total withdrawal from production business and focus on the development of a highly efficient retail chain. Both parties were confident and persuasive, both scenarios had significant risks as well as great opportunities. By 6 p.m. the discussion had exhausted itself, and now the Chairman, who was also the major shareholder, had to exercise his ultimate authority and make a hard decision whether to support one of the parties or to suggest a radically different strategy.

Kislorod Group

Founded in 1999 *Kislorod Group* was a local holding company situated in Nizhny Novgorod. The company operated in three businesses:

i) Producing and selling industrial gases (s.a. oxygen, nitrogen, carbon dioxide, etc.);

ii) Selling used cryogenic equipment;

iii) Selling welding equipment.

Though different, the three businesses were complementary as industrial gases are often kept in cryogenic tanks and used in welding. However, each of the three had specific traits and could be run separately. To provide better conditions for independent growth in each business, the single limited company had been restructured into nine separate legal entities including the Proprietary Company and the Management Company that owned seven subsidiary business units (Exhibit I and Exhibit II).

Gas Business

Producing and selling industrial gases had always been the main business for the company. Started as an intermediate seller, it grew to a solid complex group of two production sites, retail outlets across Nizhniy Novgorod region and a distribution center with overall annual sales more than 100 million RUR.

Like all the big market players Kislorod Group too had two ways of producing gases. The first way consisted of compressing and separating atmospheric air with the help of special compressor stations. The technology presumed the possibility of both filling cylinders with compressed gas as well as filling cryo-tanks with liquid gas. This required a well-equipped production ground, significant initial investment, comparatively large amount of fixed costs, and depended greatly on the price of electricity, which constituted the main portion of variable costs. The second way was to fill gas cylinders by evaporating liquid gas by means of mobile gasification equipment. Liquid gas was bought from those chemical plants and refineries where it was generated as a side product of the main production process.

The first way of production, though expensive at low production levels, had great economy of scale. It also allowed providing pipeline supply to large clients. The second way was comparatively cheaper when producing small amounts of gas, and allowed providing great mobility of production, though had certain restrictions on capacity and depended significantly on liquid gas supply, which was unstable in price and volume.

As the cost of electricity was constantly growing, many gas producers were likely to switch completely to the second way of production. This resulted in severe competition for buying liquid gas and caused a dramatic increase in price levels. Eventually evaporating liquid gases became an easy-to-enter but a hard-to-grow business.

The cost of gas transportation using motor transport was significant. It increased enormously with the increase of the distance of delivery. Pipeline transportation could be provided only for relatively short distances. Railroad delivery service also could not be widely used as it required a railway to a destination point. There was a trend of significant gradual increase in the cost of transportation of any type.

Due to aggressive sales strategy and generous re-investment policy, by the end of 200[illegible] Kislorod Group had become the largest producer and seller of industrial gases in the region. The Board wanted to gain even higher growth by challenging the strongest competitors and capturing their market shares (Exhibit III).

At the time, the gas market in Nizhny Novgorod suffered severe price competition. Although there was a sustainable growth in gas consumption, the majority of market players still held to non-differentiated marketing policy and generous discounting. That resulted in the shrinkage of actual market monetary value (Exhibit IV).

Still the increasing volume of gas consumption and the weakness of the market players attracted global international corporations, so that the Russian divisions of *Linde Gas* and *Air Liquide* expressed their intension to enter Nizhny Novgorod region. With well elaborated business processes, diminished costs, high product quality level, immense amount of resources and political influence from mother companies, these two were incomparably stronger than any local market player.

Cryogenic Equipment Business

The company had started selling used cryogenic equipment early in 2006 and through the year achieved dominant position in the market. The business model was simple. It presumed buying used cryogenic equipment from those companies that needed them no longer, then repairing it and providing the necessary service, and then selling to a client together with the necessary engineering and mounting from Kislorod's side. At the beginning of 200[illegible] the business was extremely unstable: the sales were occasional and unpredictable, the rate of operational return on sales differed from 10 to 90 per cent, and there were neither guaranteed stock nor patrons. Yet there was still a perspective for enormous growth as the market grew rapidly, and the company had not yet tried to expand the business out of Nizhny Novgorod region.

The most attractive side of the business was the fact that cryogenic equipment once introduced into a client's business processes presumed regular demand in liquid gases and technical service. But there was still not so much difference among the supply in the market.

Welding Business

At that time *Kislorod* was selling two types of welding equipment: welders and electrodes. Set up as a complementary activity to the main gas business, it finally grew into a solid business unit that contributed greatly to the overall profit. The sales were organized in two ways. The first way comprised direct sales to corporate clients, the second one constituted retail sales through *Kislorod* outlets.

The two products, though complementary, were very different. The welders were sold at average 10,000 RUR per unit, had 3 to 4 months of turnover period, low seasonal sales volatility, and were provided by a number of suppliers. The electrodes sold at 200 RUR per box, had 2 weeks of turnover period, high seasonal sales volatility, and were actually provided by a single Supplier in the central part of Russia that had a very strict dealing policy, which required the

Construction firms of different size formed the market: from private brigades to state-wide corporations. *Kislorod* sustainably held about 1/5 share of the regional electrode sales, competing with a large number of other companies, none of which though was part of a greater corporation.

The Production Strategy

The core idea of the strategy was to focus on the compressive production of industrial gases. In order to do so, it was suggested to conduct total modernization of the production site in Dzerzhinsk, which supposed the capital repair of several buildings, the acquisition and installation of new equipments, the construction of 700 meters long rail way. The ultimate goal was to establish a world-class production of industrial gases to achieve unrivaled advantages in costs and quality.

The implementation of the strategy demanded raising around 80 million RUR by selling a part of company's capital assets (such as the retail chain, the production site in Bor, and some other non-specialized assets) and receiving a 70 million RUR leasing agreement from a partner bank.

It was expected that in fourteen months the reconstructed site would be able to raise its production capacity up to 100,000 gas cylinders a month. This would be enough to reach the sustainable domination in the local market and establish a firm ground for further expansion.

The Retail Strategy

This strategy originated from the assumption that *Kislorod Group* would not be able to achieve the costs and the quality necessary to compete with the global companies. Thus, the efforts should be focused on the development of a wide-spread and efficiently manageable retail chain. In three years the chain was supposed to cover the whole Privolzhsky Federal District with no less than 30 outlets. Each outlet was implied to yield high corporate standards of service and provided a wide range of common industrial products. Besides, each outlet would be a mobile pavilion that if necessary could be relocated to a more suitable place (Exhibit V).

The strategy required no significant initial investment and in case of no emergency could be supported with regular cash flow. Turnover assets could be raised through increasing payables from suppliers and receiving short-term bank overdrafts.

An essential part of the strategy consisted in creating an efficient system of distribution. It was presumed to make an alliance with a federal distributor which would provide all the necessary logistics. However, the construction of own distribution business could be possible in three years in case the strategy had been successfully implemented.

Eventually, the strategy should help *Kislorod Group* abandon industrial gas production and become the largest retail seller of a wide range of industrial goods.

Each of the two strategies presented challenges and significant risks. However, the company

What way was to be chosen? The Chairman took a one-day period off to analyze the situati and take the right decision. He realized that the company, like never before, needed a cle vision that would unite people and lead them all to success.

Exhibit I: Kislorod Group

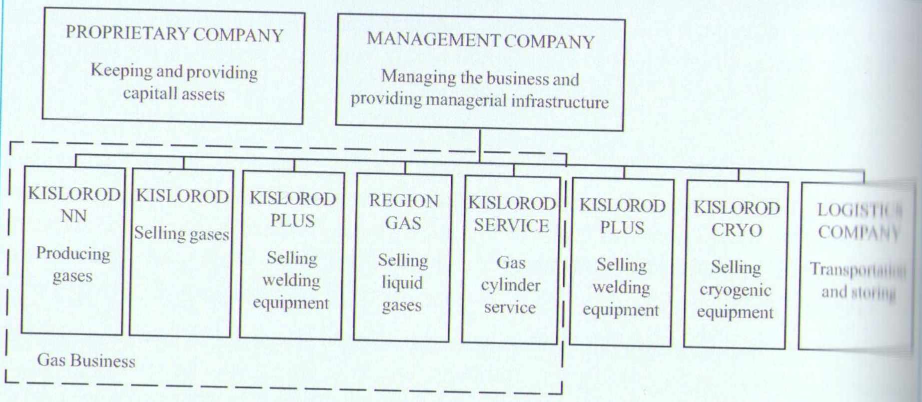

Exhibit II: Average Monthly Financial Figures of Kislorod Group (in thousands RUR)*

Business Unit	Total Revenue	Fixed Costs	Variable Costs	Number of Employees
Kislorod	6 200	1 400	4 400	46
Kislorod Plus	3 600	600	2 480	5
Region Gas	4 000	100	3 500	7
Kislorod Service	400	100	200	9
Kislorod Cryo	3 100	400	1 700	21
Kislorod NN	-	2 300	1 000	58
Logistics Company	-	1 400	600	14
Proprietary Company	-	300	0	2
Management Company	-	2 100	0	36
TOTAL	17 300	8 700	13 880	198

* Kislorod NN, Logistics company, Proprietary Company and Management Company do not generate revenues from outside markets.

Exhibit III: Main Players of the Industrial Gas Market in Nizhny Novgorod Region (2007)

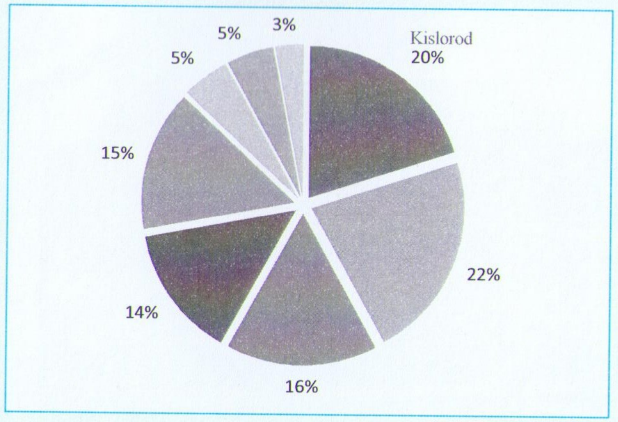

Exhibit IV: Shrinkage of the Monetary Value (in million RUR per year)