

# Making Purchasing and Inventory Strategic

— *An Essential to Mining Success*

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It's the glory days in coal mining. Top companies are driving mining productivity and profitability through radical transformation of their purchasing and inventory philosophies, practices, and results. Double-digit productivity improvements and cost reductions are fueling coal mining's profit potential.

**C**oal is back! And soon to be king once again. Over the last two years, dramatic increases in coal demand and price have polished the black rock to gold. Adding to coal's allure are the continued demands for clean energy and the economic damage from high natural gas and oil prices. "It's an exciting time," says Bill Richards, Vice President Company Wide Purchasing and Inventory, United Coal Company. "We've learned full productivity at the face requires having a purchasing and inventory strategy in place that aligns our company's supply-side direction and drives exceptional performance from suppliers." Talk about mining for gold, strategic purchasing and inventory can lead to double-digit price/cost reductions—impressive results given today's tough supply-side marketplace.

How tough is it? The last two years have brought drastic price increases in metals, fuels, lubricants, and rubber products. Coupled with the supply scarcity, internal resource constraints, and untrained suppliers, having a purchasing strategy is essential. "Strategic purchasing leverages time, talent, data, processes and volumes. It's a cross-functional, continuous improvement approach that knows how to satisfy customers and measure, capture, and execute on a lowest total cost basis," says Steve Trecha, President and CEO, Integrated Strategies, a mining supply chain consultancy. Without a strategy, maintenance workers can spend up to 40% of their time hunting for parts, while expensive capital equipment assets sit idle. With a strategy, face productivity soars.

Purchasing and inventory as strategic—for many it's a dichotomy. Traditionally, purchasing and inventory

processes have been fragmented with departments viewed as exception processors and store keepers. "In the past, being a tactical buyer was the norm—today that's not acceptable," says Richards. "As a purchasing person, it's too late to bring value if you wait for the requisition to cross your desk. To be truly effective, purchasing must be joined at the hip with both users and suppliers. The result

is increased mining productivity, drastically reduced cost of operations, and improved working relationships and employee morale."

"Under the watchful eye of owners and investors, coal senior management can no longer tolerate the lone cowboy and traditional fire fighting mode," notes Trecha. Purchasing and inventory strategies must be closely tied with mining plans. Suppliers must operate as integral business partners and be incentivized to achieve mine production goals. Best practice suppliers understand their success is determined by their mining customers' success. Consequently, they work to demonstrate value every day.

Departmental turf issues and the ability to bring together disparate mining divisions can be an obstacle. "In many cases," notes Trecha, "what was previously interpreted as control issues were simply managers lacking data and a decision process they could trust." Key decisions in purchasing and inventory include which supplier to use, material performance expectations, price to pay, responsibilities for continuous improvement and cost reduction, supplier performance, inventory investment, and the acceptable supply-side costs to do business. "With a strategy in place, these considerations are addressed cross-functionally. Management has continued visibility and

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participation,” notes Richards. “It’s important to clarify purchasing doesn’t own these decisions. Purchasing drives the cross-functional integration, and is responsible for getting the right players involved to make decisions on a lowest cost basis.”

Reflecting on a past mining operation in the Appalachian corridor, Richards says, “One mine produced 3.8 million tons of coal a year. Our inventory investment was near \$4.8 million. The mine was targeted for big growth. But it was apparent our purchasing and inventory processes would not support the growth. We launched a purchasing and inventory transformation at the same time the mine expansion was happening. As a result, our spare parts inventories were reduced by over 75%. We ended up with a \$1.2 million inventory supporting a 7 million ton operation. Best of all, mine productivity increased at the same time.”

Traditionally, users see inventory reduction programs as a risk to parts availability. Yet firms who operate their inventory programs strategically find there is no risk, and reap the full benefits. For example, with a strategic inventory program it’s not uncommon to achieve work crew productivity improvements of 20-40%, equipment uptime increase of 5-15%, and overall internal customer responsiveness improvements of 30-80%. “These are impressive and real numbers,” adds Trecha. “It’s a win-win-win-win for operations, maintenance, suppliers and coal customers.”

“We’ve almost come full circle,” states Bill Richards. “In the past, it was a struggle to get suppliers involved with cross-functional teams. We had to work hard to help suppliers understand how to work with us to reduce total costs versus simply reducing purchase order pricing. Today, our suppliers seek out cross-functional teams to

help improve mining productivity and drive cost out.” Trecha adds, “Suppliers face the same challenges as their mining customers. Whether responding to drastic price increases or resource shortages, suppliers too must take cost out of their business.”

How do the best firms in the industry make this happen? “It starts at the top,” says Richards. “Senior management must establish the vision and expectation that a purchasing and inventory strategy is a cross-functional way of driving alignment and cost reductions.” Trecha refers to it as “coordinated company wide sourcing and inventory.” “It’s a systematic, aggressive and leveraged approach to improving mine productivity and reducing the cost of operations on a year over year basis. It is customer focused, recognizing the true mining customer is not maintenance or operations—it’s the equipment. By keeping the equipment running at optimal health, the probability for achieving work crew productivity and capital utilization goals are markedly increased.” Adds Richards. “It is not enough to say purchasing and inventory are strategic. There must be measurable results demonstrating bottom line performance at the mine level.”

The transition to strategic must be transformational. Transformations target behavior changes and ways of doing business that are sustainable over time. “Anything less looks like purchasing’s tired approach of beating up suppliers on price and shouting for inventory reductions,” says Richards. The vision must be believed, communicated, and followed by top management. “You know management is engaged when they look to the outside to bring in new ideas and change management techniques that establish sustainable results,” says Trecha. Management meeting agendas squarely place purchasing and inventory improvements on the same level with safety and production.

Many firms struggle with common dynamics when

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growing and attempting a purchasing transformation at the same time. Pushback, resource constraints, changes in behaviors, and understanding how to capture and use data to make business decisions are typical and expected. These factors alone sometimes drive mining companies to give up their there supply-side improvements assault.

In response, Integrated Strategies developed the three-step Roadmap to Strategic Sourcing Success Template. Used across dozens of companies and multiple industries, it is a benchmarked approach that is driving real business results in the mining industry.

The first step to Strategic Sourcing Success is setting transformation expectations and establishing personal accountabilities. Trecha explains, “Opportunities should be quantified and qualified with a vision and plan to capture them. A simple test to understand if your company is ready to go the next step is to ask: Has a sourcing vision been ratified by cross-functional executives? If the answer is no, more work needs to be done before you proceed.”

The process continues with identifying performance measures. Solid measures that reveal the true value of the effort must be put in place. This step involves two parallel pathways. The first is aggressively pursuing competitive and tactical activities that bring quantifiable business results. Examples include increasing parts visibility in a warehouse, working on supply assurance in a particular commodity, or optimizing inventory. These activities bring immediate mine operation improvements. The second parallel effort involves developing and deploying a transformational infrastructure. This includes establishing a cross-functional leadership team focused on opportunity alignment and resource allocation. Working in parallel, this dual approach brings immediate value while driving sustainability (see Exhibit I).

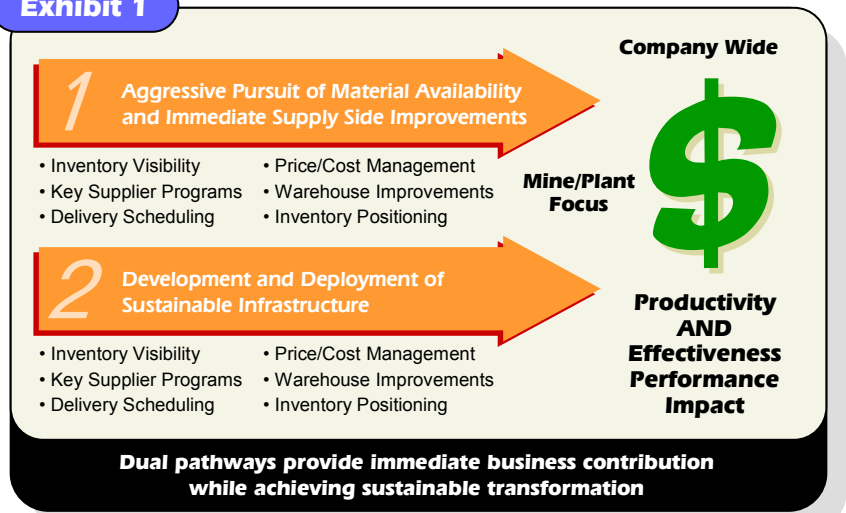
The last step involves developing processes and structure. This includes organizational design plus policy and system review. “Most organizations work it backwards,” says Trecha. “They reorganize the company and buy new computer systems before they understand how business will be conducted. In the transformational approach, philosophies, accountabilities, non-negotiables, and performance metrics drive success.” As author Dr. Stephen Covey puts it, “Work first on principals, then behaviors.”

The results are double-digit price/cost reductions and improved mining productivity. Equally important is an enhancement in esprit de corps and a reduction in personal frustrations. “There’s no question the transformation

approach brings significant business results, yet an often overlooked benefit is personal job satisfaction that results from training people how to work together more effectively,” says Trecha. “Operating strategically, our organization tackles tough supply-side problems quicker, and our people actually enjoy doing it. They are having fun,” adds Richards.

The current pressure to reduce reliance on foreign oil and natural gas ideally positions coal, the United States’ most abundant and secure energy resource, as a viable alternative. With growth and expectations for productivity and profitability building, strategic purchasing and inventory should be a mainstay in any mining executive’s toolbox. Notes Richards, “What’s really exciting is there are no heavy capital investments to achieve the benefits of strategic purchasing and inventory.” Dollars spent are typically in external assessments, coaching, and training while real results are being achieved. “The payback typically ranges from \$5-\$20 returned for every dollar invested,” says Trecha. “It’s dynamic, proactive and critical to mining success,” adds Richards. “United Coal is not missing out on this coal boom, or the benefits of strategic purchasing and inventory.”

**Exhibit 1**



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**Success is  
the only  
option!**



Supply Chain

Strategic  
Sourcing

Logistics

Materials  
Management

Order  
Fulfillment

Six-Sigma

Initiative  
Management

## Qualifications

- Consultants average more than 20 years experience
- Web-Based strategic sourcing tools
- “Concept to Reality” approach
- Hands-on implementation
- Worked with more than 200 firms across multiple industries
- Developed more than 250 supply chain and logistics strategies
- Integrate core supply chain with core business strategy

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