LOFTIN DISTRIBUTION IN 2010

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Loftin Distribution[1] was a family-owned industrial distribution firm organized as a partnership and headquartered in Dallas, Texas (Table 1). The company was formed in 1945 as an automotive wholesale business. Over time, it evolved into a bearings and power transmission distributor. During the company's 2003 strategic planning activity, its managers recognized that the mechanical power distribution business was mature and that Loftin needed to become more diversified. It then broadened its product line and began selling more products to the existing customer base. Its CEO, Bob Loftin, described the company as "helping its customers to meet their materials handling needs" (Table 2).[2] [3]. Loftin's net revenues in 2008 and 2009 were $122.3 million and $100.4 million, respectively. (Table 3)[4] Bob Loftin's vision for the company was that, by 2012 or 2013, it should become the largest independent power transmission distributor in the United States with sales around $300 million[5]

Loftin's Products

Loftin distributed industrial products through agreements with some of the best manufacturing companies in the U.S. The market in which Loftin competed had four levels of price and quality. Loftin sold at the high end of the market, emphasizing the high quality of the products and services provided. Products sold included conveyor belts, pulleys, gearboxes, bearings, and electrical motors. Services provided to customers included installation, repairs, and routine preventive maintenance.[6]

Loftin's operations were organized into seven strategic business units (SBU's):

- Loftin Bearing Service, a distributor of bearings, seals, power transmission components, and geared products;
- CapCorp Total Belting Solutions, a field service organization that sold, installed, and repaired conveyor belts;
- Triad Industrial Automation, specializing in motors, drives, sensors, and industrial controls;
- American Keyed and Custom Shafts, manufacturer and supplier of plain, keyed, and custom shafts;
- U.S. Conveying Systems and Equipment, which assisted customers with bulk material handling systems, screw conveyors and bucket elevators;National Mechanical Power Systems, distributor of large enclosed gear reducers and other engineered products; and

- HydraAir Fluid Power Products, which sold pneumatics components, hydraulics components, connectors, and full system design.

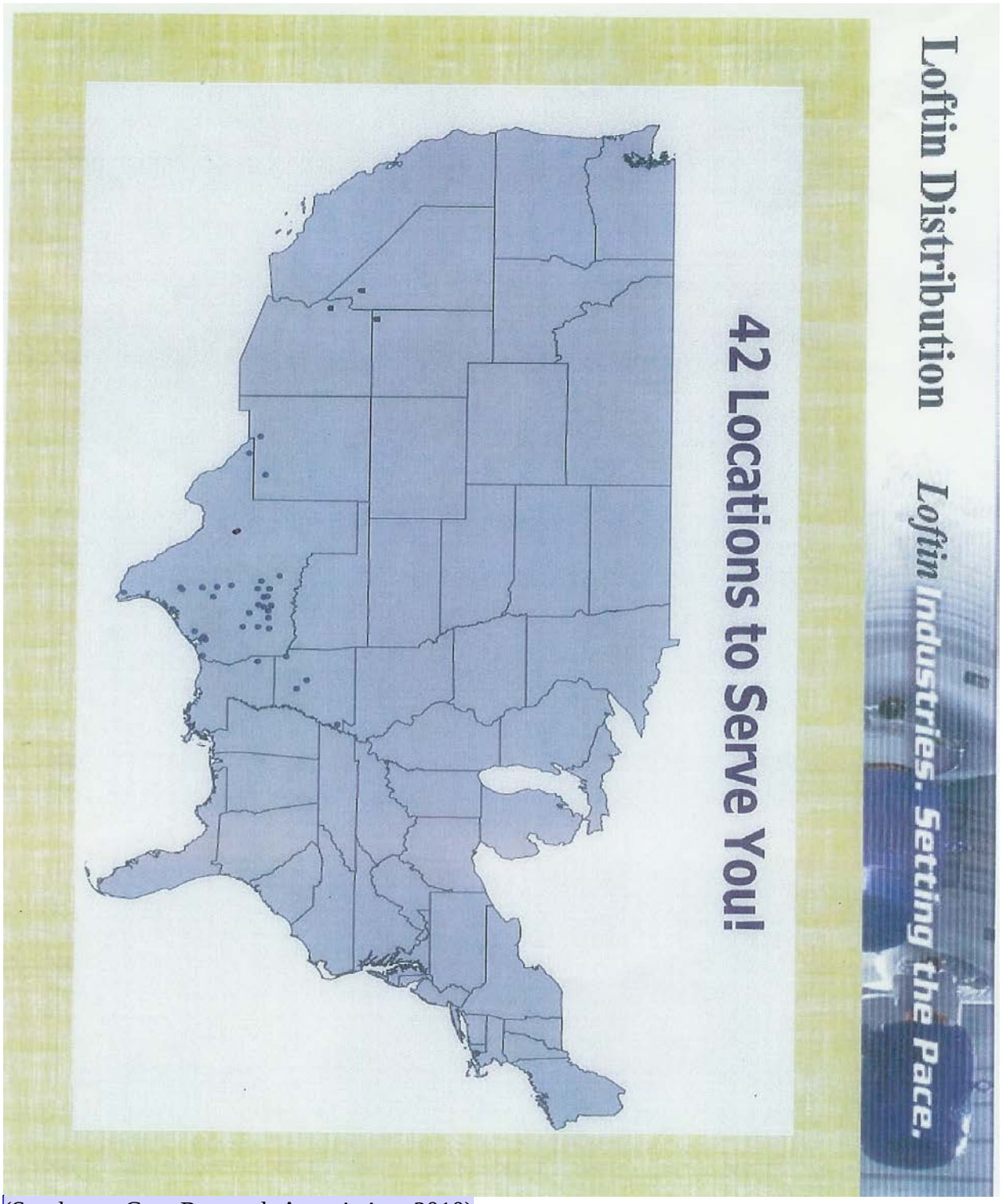
Table 1
Loftin Distribution
Headquarters and Primary Distribution Center
Dallas, Texas

Number of locations	42
Distribution of locations	Texas (32 locations), Arkansas, Louisiana, New Mexico, Arizona, Nevada, Utah
Number of employees	360
Sales for fiscal year 2009	$100.4 million
Number of SKU's in stock	28,000
Number of items it can sell	250,000
Customers' industries	Aggregate, food processing, oil and gas, lumber, waste water processing, car shredding
Example suppliers	Timken, Martin Engineering, Fenner Dunlop, Baldor, ABB, Eaton
Products and services	Bearings, seals, conveyor belts, motors, drives, shafts, bulk materials handling systems, gear reducers, pneumatic and hydraulic components

(Southwest Case Research Association, 2010)

See company locations in Figure 1 on the following page.

Figure 1 – Company Locations



(Southwest Case Research Association, 2010)

Table 2
Loftin's Management and Culture

Loftin's top management team (see Organizational Chart in Figure 2):

- Bob Loftin, President and CEO
- Cameron Barker, Vice President of Corporate Operations
- Bob Moran, Vice President of Finance
- Stacy Mikkelsen, Vice President of Sales & Marketing
- Allan Ross, Vice President of CapCorp Sales & Operations

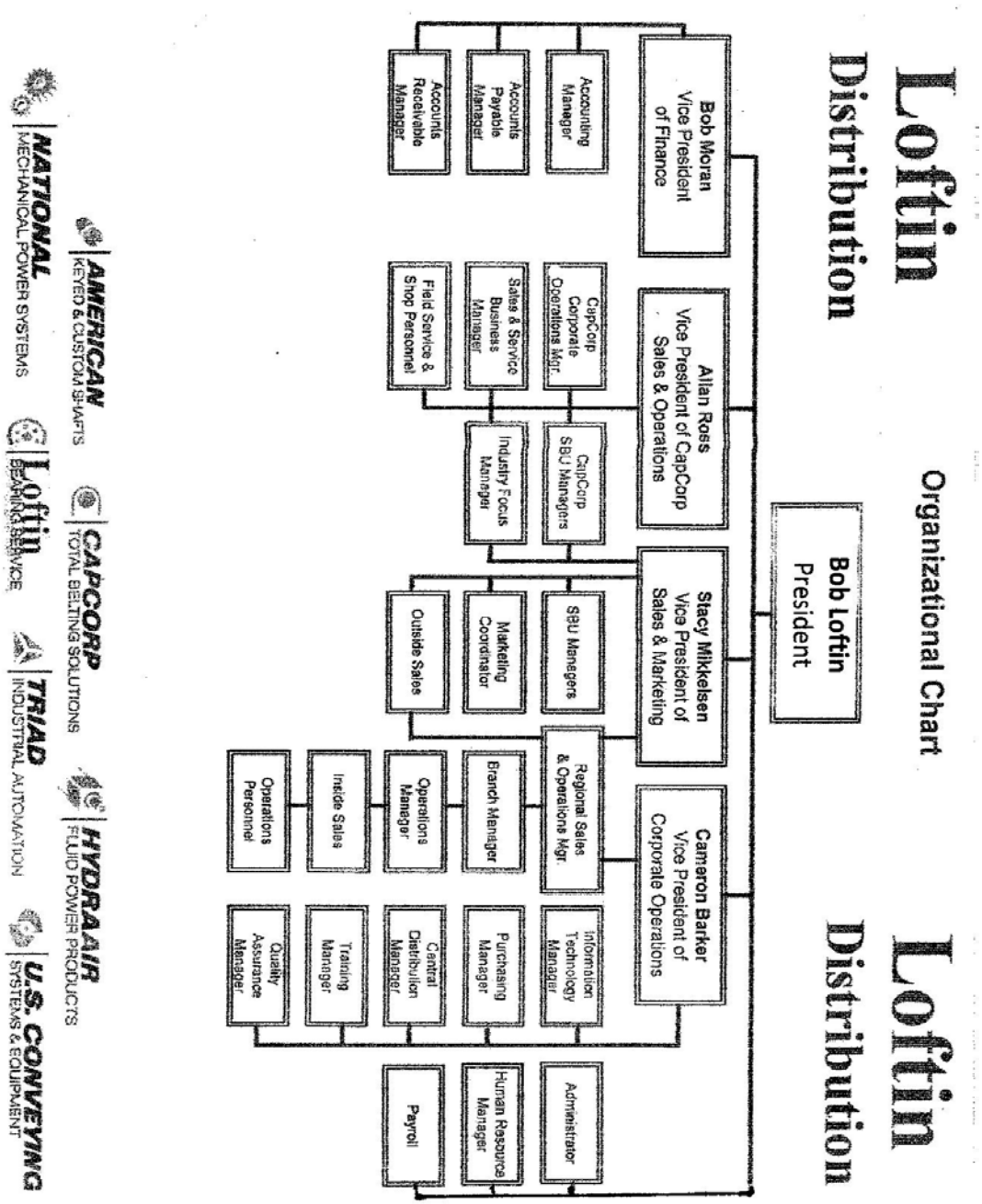
Cameron Barker said that how Loftin did business is about "how do we meet the customer need, not about the lowest cost product, but providing the lowest cost of total ownership to customers".[7]

Several key people, including Bob Loftin, were former military. Loftin went into the military soon after graduating from high school. After six years in the Navy, he came back in 1973 to help run the family business. Perhaps as a result of his military background, the company culture emphasized discipline and a high level of ethics and integrity.[8]

Loftin Distribution was formed by Bob Loftin's father and uncle in 1945. Bob Loftin knew almost all the employees in the company. The organizational structure was not rigidly enforced – almost any employee could go to Bob Loftin when there was reason to do so. Loftin had 3 daughters. The youngest was not in the business in any way. One daughter worked in the business (in accounting), as did two sons-in-law (husbands of the two older daughters). The company did not have a formal succession plan.[9]

(B. Loftin, interview, March 4, 2010; C. Barker, interview, March 4, 2010)

Figure2
Loftin Distribution Organizational Chart



(Southwest Case Research Association, 2010)

Table 3

Loftin Distribution – Financial Highlights
(dollar amounts in thousands)

Yr. ended 12/31	2009	2008	2007	2006	2005	2004
Sales, net	$100,356	$122,253	$117,534	$100,568	$80,606	$69,870
Gross profit	31,689	39,634	37,719	31,111	23,971	19,968
Gross profit as a percentage of sales	31.6%	32.4%	32.1%	30.9%	29.7 %	28.6%
Net income	$6,525	$15,020	$14,341	$10,718	$5,506	$2,293
Net income as a percentage of sales	6.5%	12.3%	12.2%	10.7%	6.8%	3.3%
Total assets	$54,328	$56,479	$44,360	$38,611	$34,223	$30,564
Total liabilities	5,455	10,940	8,416	11,464	13,592	12,998
Partners' capital	48,872	45,538	35,944	27,147	20,632	17,565
Cash flow provided by operations	12,443	11,479	12,284	8,200	2,845	1,362
Net increase (decrease) in cash	2,897	611	326	(220)	635	5

(Southwest Case Research Association, 2010)

Loftin's SBU's were run by degreed engineers, to provide customers better, more knowledgeable services, and more engineering services.[10] Its inside and outside sales people had years of experience in the industry; on average, they had been with the company for 12 to 15 years. Providing better, more advanced services allowed Loftin to get higher gross profit margins than its competitors.[11]

At the end of 2009, the company had 42 locations: 33 in Texas, most of which were in the eastern half of the state; 3 in Arkansas; 2 in New Mexico, and one each in Arizona, Nevada, Utah, and Louisiana. Six of the locations were for the operations of CapCorp Total Belting Solutions, while the remaining locations provided customer access to the products and services of the other SBU's. Loftin's distribution center was located in Dallas.[12]

Loftin's Customers

Loftin's customers fell into in two broad categories: original equipment manufacturers (OEM) and maintenance, repairs, and operations (MRO). Loftin sold to its OEM customers parts that they used in making their products (such as bearings and electric motors). For MRO customers, Loftin provided parts and services that they needed to keep their facilities running. Table 4 shows the breakdown of Loftin's sales by category of customers.

Table 4
Loftin's Sales by Category of Customers

Year	OEM side of the business	MRO side of the business
2003	20 – 25 percent of sales	75 – 80 percent of sales
2008	35 – 40 percent of sales	60 – 65 percent of sales

(B. Loftin, interview, March 4, 2010)

From 2003 through 2008, the MRO side of the business grew, but OEM sales grew more rapidly. The OEM side of the business was more cyclical, more sensitive to overall economic conditions. Therefore, the increased percentage of OEM sales in the company's sales mix caused the recession of 2008 and 2009 to hurt more.[13]

For MRO sales, the customer's downtime was critical; the greatest cost to the customer was not the cost of the part it purchased, but the production lost while the system was down. Bob Loftin believed that the parts sold to MRO customers were mission critical parts and that the quality of the parts was more important than the cost. Therefore, Loftin positioned itself at the top end of the market, selling top quality parts. Its goal was not to provide the lowest cost product, but to provide the lowest total cost of ownership to customers.[14]

Loftin's customers were aggregate companies, food processing businesses, oil and gas companies, lumber companies, waste water processors, car shredding companies, and anybody who made anything. Aggregate was the largest category of sales for Loftin, at 25 to 30 percent of total sales revenue. "Aggregate" referred to companies in cement, concrete, road work, rock, coal, and copper mining. At the end of 2009, aggregate companies were expecting to benefit from the federal government's economic stimulus package, but the stimulus had not yet kicked in for this industry. Oil and gas was the second largest sales category for Loftin at about 20 percent of sales, mostly located in the Houston area. Third largest was industrial operations companies, such as car shredding businesses. While sales to most customers were down in 2009, sales to food processing and agricultural customers were not affected as much by the recession.[15] To provide fast, reliable delivery to customers, Loftin promised to deliver products 24/7. Loftin placed its product as close to the customer as possible, so it had a large amount of inventory at each of its locations to serve customers better. Carrying so much inventory reduced the company's inventory turnover but allowed Loftin to charge a higher price for its product and generate a higher gross margin. Loftin operated a fleet of delivery trucks, delivering products to the customer at no additional cost to the customer.[16]

Loftin's Suppliers

Loftin kept 28,000 different items (stock-keeping units) in inventory. Through agreements with suppliers, it could price and sell 250,000 items. It carried products from dozens of different top-of-the-line manufacturers through non-exclusive distribution agreements. Examples of some of Loftin's suppliers are shown in Table 5, listed by strategic business unit.

Table 5 Examples of Loftin's Suppliers	
Strategic Business Unit	**Examples of brands of products sold**
Loftin Bearing Service	Timken Bearings, Dodge, McGill
CapCorp Total Belting Solutions	Martin Engineering, Fenner Dunlop
Triad Industrial Automation	Baldor, Marathon Electric, Leeson, Sterling Electric, ABB
American Keyed and Custom Shafts	
U.S. Conveying Systems and Equipment	Martin Engineering
National Mechanical Power Systems	Rexnord
HydraAir Fluid Power Products	SMC. Gates, Eaton

(B. Loftin, interview, March 4, 2010)

Pricing and rebates from suppliers were critical to Loftin's profitability. The company got both quarterly and annual rebates from its suppliers. It purchased aggressively: on a $100,000 order, its purchasing department might ask the supplier for a 10 to 15 percent discount[17] If the company could grow as much as Loftin wished, it would receive more favorable pricing and greater rebates from suppliers; the amount of rebates sometimes was based on the increase in purchases over the preceding year. In addition, Loftin's advertising often was reimbursed by suppliers. Suppliers provided support for the company's website, events such as golf tournaments for customers, brochures, calendars, and print advertisements.[18]

Loftin's products came almost exclusively from U.S. manufacturers because the company's managers believed these products were higher quality and better able to meet its customers' needs. Loftin might have been able to get less expensive parts from international companies and might have been able to mark up those parts to generate the same percentage gross profit – but the dollar amount of gross profit would have declined. Bob Loftin said that "…gross profit dollars pay the bills at the end of the day"[19] . While international parts generally had a lower quality reputation, the quality of products made in China had improved in recent years. Bob Loftin expected that in coming years, U.S. industrial distributors would have to deal with increasing competition from China.[20]

The Effect of the Recession

The decrease in Loftin's sales from 2008 to 2009 mirrored the effects of the recession on the industrial distribution industry.[21] For the industry as a whole, the volume of sales depended on the operating levels of its customers; when manufacturing slowed down, the need for parts and maintenance decreased.[22] The performance of industrial distribution companies correlated with the Manufacturing Capacity Utilization (MCU) index, published by the Federal Reserve Board. One of Loftin's competitors estimated that its sales moved with the MCU when it was dropping and lagged the MCU when it was on the rise. The decline in sales for the industry began late in 2008 and continued in 2009. Bob Loftin estimated that for 2009, MRO sales were down 10 to 12 percent industry-wide, and OEM sales were down more than 24 percent.[23]

Loftin Distribution responded to the recession by pulling back some on purchasing and the amount of inventory it carried, but some of its competitors decreased their inventory more sharply. The company did not change its credit policy, but the amount of accounts receivable did contract in 2009 because of the recession. Loftin did not lay off any employees; some competitors did. In fact, Loftin added people during the recession: it wanted to be ready for the recovery. [24]

The recession led some small distributors to close down and some larger distributors to close some locations or reduce their range of products and services. A survey conducted by *Industrial Distribution* found that one out of three distributors would have welcomed an acquisition offer during this time, and several mid-sized distributors (sales in the range of $10 million to $20 million) indicated interest in growing through acquisitions, despite the recession. Some distributors created purchasing groups or other alliances to help them compete more effectively against the large distributors. For example, Bob Loftin founded the National Industrial Distributors Alliance, a best practices group that sought to provide support to independent distributors nationwide.[25] [26][27]

Some distributors responded to the recession by using the slow time to get ready for the recovery. One way to prepare for the recovery was to make changes related to technology. Some companies updated their websites to make them more user-friendly and by adding advanced features, such as streaming video. Other distributors began using customer relationship management software, which allowed them to track customers' buying habits and analyze customer profitability. The adoption of enterprise resource planning software allowed distributors to improve purchasing decisions, do more sophisticated forecasting, estimate delivery times, and increase inventory turns.[28]

The Growth Imperative

Since 2003, Bob Loftin had aggressively pursued growth of the company. He did not aspire to have a national footprint or any international operations because he believed that independent distributors like Loftin could do a better job of serving and solving problems for small and mid-sized customers than could large, incorporated distributors.[29] Initially, Loftin sought to grow through greenfielding (organic growth; growth achieved through starting new locations from scratch). The company evolved from organic growth to growth by acquisition, acquiring smaller, independent distributors. This change in strategy was based on results: greenfields generally were not profitable until the third year, while an acquired business might be profitable within a year. [30] The acquisitions were financed short-term using the company's line of credit and long-term through cash generated by the businesses.[31]

Loftin acquired a total of ten businesses over the period 2003 through 2008. An important example was the acquisition of Bearing Belt Chain late in 2008. Bearing Belt Chain, headquartered in Las Vegas, NV, was a three-location independent distributor specializing in power transmission components with a business model characterized by personal service and flexibility. The company's culture and product line matched those of Loftin, and the deal expanded Loftin's reach into Nevada, Utah, and Arizona.[32]

Loftin sometimes learned about acquisition targets from its suppliers – other industrial distributors bought from the same suppliers. In making acquisitions, Loftin was looking for people (employees) and market share. Therefore, an acquisition target needed to be in good shape financially.[33] Because Loftin sold at the high end of the market, it looked for acquisitions that provided high quality products and services and valued ethical business practices.[34] A business that was acquired by Loftin had to adopt the company's culture and systems. Sometimes, employees from other Loftin locations were moved to the new location to help with the transition. The company tried to learn best practices from the businesses it acquired and then incorporated those practices organization wide.[35]

In the early days of its acquisition strategy, Loftin sometimes worked on just a few acquisitions at a time, spending as much as three or four years on due diligence and observing the acquisition target. Later, it kept as many talks going at a time as possible. Bob Loftin then hired a professional intermediary firm to do many of the acquisition-related activities. He hoped that the intermediary would allow the company to accelerate its rate of successful acquisitions: late in 2009, Loftin missed out on an important acquisition in Oklahoma, an area the company has pinpointed for growth. The negotiations had been going well, but then the acquisition target was purchased by one of Loftin's larger competitors. Employing the intermediary would also allow Loftin managers to focus on running the existing businesses.[36]

The Industrial Distribution Industry

The managers of Loftin Distribution identified as its major competitors Motion Industries (MI), Applied Industrial Technologies (AIT), Kaman Industrial Technologies (KIT), and DXP Enterprises.[37] All were substantially larger than Loftin and were publicly traded. The industrial distribution industry was highly fragmented: the big three (MI, AIT, and KIT) plus DXP and Loftin made up about 15 percent of industry sales. There were a huge number of small, independent companies, some of which were highly specialized. Total annual sales for materials handling distributors were about $48 billion.[38]

Most industrial customers purchased supplies and parts from many different distribution and supply companies. Distributors traditionally provided their customers with repair and maintenance services, parts and equipment, and technical support for one product category or a limited range of categories. For example, a customer might have acquired its conveyor belt service and parts from Loftin but most of its other industrial supplies and services from other distributors. In an attempt to lower total purchasing costs and improve inventory management, some customers had reduced the number of supplier relationships they maintained.[39] In response, industrial distributors were increasing the number of product lines they carried, which contributed to the consolidation observed in the industry since 2000. Generally, the distributor purchased products directly from the manufacturer and warehoused them at its distribution facilities until sold to the customer. Distributors had non-exclusive distribution agreements with manufacturers; as a result, a particular brand might be carried by many distributors. Often, the distribution agreements, which were cancelable by either party, had been in effect for many years. Manufacturers did make some sales direct to the customer. Generally, these sales were

large-volume purchases made by original equipment manufacturers. For MRO transactions, the manufacturer generally directed the customer to one of its distributors.

Industrial distribution was highly competitive. Historically, there had been few economic or technological barriers to entry, leading to the high fragmentation of market share. Competition in the industry was based on the breadth and quality of products and services, the availability of products, the ease of product selection and ordering, and having a local presence. Competitive advantages for a particular distributor might include long-term relationships with suppliers and customers, geographic coverage, and name recognition.

Sales and profitability for an industrial distributor were highly sensitive to economic conditions influencing the distributor's customers. All of the distributors referred to in this case experienced sharp declines in sales beginning in late 2008 and continuing into 2009, as their customers scaled back operations due to the recession. Sales to customers in most industries decreased; the industries least affected by the recession included food production and power generation. The recession impacted the selling prices and terms of sale demanded by customers and the incentives and rebates offered by suppliers. The industry was also affected by the long-term trend of its customers moving some operations overseas, reducing the overall market opportunity in North America.

The Competitors

Applied Industrial Technologies. Applied Industrial Technologies (AIT) described itself as "one of North America's leading industrial product distributors."[40] (See Table 6 and Appendix 3). The company sold both MRO and OEM parts and services. AIT had 2 reportable segments, both providing products and services similar to those offered by Loftin: service center-based distribution and fluid power businesses. The service center-based distribution (SCBD) segment provided a wide range of industrial products through service centers across North America. Most sales were for customers' scheduled maintenance of their machinery and equipment and for emergency repairs. AIT also operated regional fabricated rubber shops that modified and repaired conveyor belts and made hose assemblies. SCBD accounted for most of AIT's field operations and 83 percent of its 2009 sales. The fluid power businesses segment consisted of specialized regional companies that distributed fluid power components, assembled fluid power systems, and repaired equipment.[41]

Table 6
Applied Industrial Technologies
Headquarters: Cleveland, OH

Number of locations	More than 460
Distribution of locations	47 states (includes 22 locations in Texas), Canada, Mexico, Puerto Rico
Number of employees	4,700
Sales for fiscal year 2009	$1.9 billion
Number of items it can sell	3,000,000
Customers' industries	Aggregate, automotive, government, HVAC, cement, mining, energy efficiency, petrochemical, ethanol production, pharmaceutical, power generation, food processing, wastewater treatment
Example suppliers	Timken, Dodge, 3M, Baldor, Eaton, Fenner
Products and services	Fluid power systems, equipment repairs, adhesives, bearings, hydraulics, pneumatics, safety products, industrial hose and fittings

(Applied Industrial Technologies, 2009 and 2010)

AIT's goal was to help customers minimize production downtime, improve machine performance, and lower their procurement and maintenance costs. The company maintained product inventory levels at each service center tailored to meet the needs of the local market. Prompt delivery of products was critical, particularly for emergency repairs. AIT also offered its customers an automated storeroom replenishment system, AppliedSTORE®, intended to help customers improve the tracking and management of maintenance and repair supplies.[42]

Because most industries served by AIT were mature, growth since 2000 had come primarily from acquisitions. For example, in 2007, AIT acquired the largest independent fluid power distributor in Mexico. AIT hoped to continue its acquisition strategy, growing the business in North America within its existing range of products.[43]

DXP Enterprises. DXP Enterprises (DXP) provided maintenance, repair and operating products, equipment and service to industrial customers.[44] (See Table 7 and Appendix 4.) At end of 2009, DXP was organized into two segments: MRO and Electrical Contractor; the small Electrical Contractor segment was disposed of early in 2010.[45] With its headquarters in Houston, DXP had particularly strong ties to the oil and gas industry; its sales tended to go up and down with the level of activity in the oil patch. DXP's product line was influenced by the needs of oil and gas producers. For example, DXP's website emphasized pumps of various types.[4647]

Table 7
DXP Enterprises
Headquarters: Houston, TX

Number of locations	169
Sales for fiscal year 2009	$445 million
Number of SKU's	45,000
Number of items it can sell	1,000,000
Customers' industries	Oil and gas, general manufacturing, petrochemicals, wood products, mining, construction
Example suppliers	Viking Pump, Timken, Loctite, Gates, 3M, Goulds Pumps, Eaton, Dodge
Products and services	Fluid handling equipment, bearings, power transmission equipment, safety supply, pumps, electrical products, integrated supply program

(DXP Enterprises, 2009; DXP Enterprises, 2010e)

DXP's growth strategy involved the acquisition of businesses with complementary or desirable product lines, locations or customers. The company completed 13 acquisitions from 2005 through the end of 2009. These acquisitions included a pump remanufacturer; geographic expansion into in Ohio, Indiana, Kentucky, West Virginia, New Mexico, Colorado, and Texas; an acquisition to strengthen DXP's position with oil and gas and pipeline customers; two distributors of safety products; a distributor of welding supplies; and a distributor of fasteners.[4849]

DXP offered SmartSource®, a proprietary integrated supply program that allowed a customer to outsource its purchasing, accounting and warehouse management to DXP. DXP expected that customers who used the program would increase the share of their purchases made from DXP. [50]

Kaman Industrial Technologies. Kaman Corporation operated in two industries: aerospace and industrial distribution (Table 8). Its industrial distribution segment was Kaman Industrial Technologies (KIT). KIT described itself as the third largest 'power transmission/motion control industrial distributor in North America (Table 9 and Appendix 5).'[51]

Table 8

Industries in Which Kaman Corporation Operated**Percentage of consolidated net sales**	**2009**	**2008**
Industrial distribution	56.3 percent	62.0 percent
Aerospace	43.7 percent	38.0 percent

(Kaman Corporation, 2009)

In 2009, KIT experienced continuing weakness in some markets and industries that had begun in late 2008. The downturn, caused primarily by a significant decrease in sales to OEMs and reduced capital spending by MRO customers, had a significant impact on KIT's results. Lower sales reduced the company's ability to leverage its operating costs. In response, it undertook careful cost reduction activities.[52]

Table 9
Kaman Industrial Technologies
Headquarters: Windsor, CT

Number of locations	Nearly 200
Distribution of locations	43 states (including 7 locations in Texas), Puerto Rico, Mexico, and Canada
Sales for fiscal year 2009	$646 million
Number of items it can sell	3,000,000
Customers' industries	Power generation, wood products, robotics, food and beverage processing, mining, machinery manufacture
Example suppliers	Baldor, Dodge, Timken, Gates, Dow Corning, Loctite
Products and services	Bearings, power transmission, electrical, materials handling, linear motion, fluid power, inventory management

(Kaman Industrial Technologies, 2010)

KIT's strategies included expanding its geographic footprint in major industrial markets to allow it to compete more effectively for regional and national accounts. KIT's managers had found that customers with national and international operations preferred to deal with distributors that had similar geographic range.[53] [54]

In February 2010, KIT announced that it had acquired 2 distributors: Fawick de Mexico SA of Mexico City and Allied Bearings Supply Co. of Tulsa, OK. The acquisition of Fawick, a distributor of fluid power and lubrication products, equipment and systems, demonstrated KIT's intent to increase its presence in Mexico. Allied was a distributor of bearings, power transmission, material handling and industrial supplies with eight branches, six of them located in Oklahoma. T. Jack Cahill, president of KIT, commented that "This acquisition reinforces our stated commitment to balance organic growth with strategic acquisitions that help us to increase our scale and fill our geographic footprint." [55]

Motion Industries. The parent company of Motion Industries (MI) was Genuine Parts Company (GPC), which was engaged in distribution of automotive replacement parts (through its automotive parts group, NAPA), industrial replacement parts (through MI), office products (through its office products group, S. P. Richards), and electrical/electronic materials (through EIS).[5657] (See Table 10 and Appendix 6.)

Table 10
Motion Industries
Headquarters: Birmingham, AL

Number of locations	501
Distribution of locations	46 states (including 37 locations in Texas), Puerto Rico, Mexico, Canada
Sales for fiscal year 2009	$2.9 billion
Number of SKU's	80,000
Number of items it can sell	4,000,000
Customers' industries	Food processing, primary metal, mining, petrochemical, forest products, paper, automotive, pharmaceutical, power generation, wastewater management, wind and solar power
Example suppliers	ABB, Baldor, Dodge, Dow Corning, Emerson, Fenner, Timken
Products and services	Bearings, industrial automation, industrial supplies, hydraulic and pneumatic components, mechanical power transmission, hoses and fittings, materials handling

(Motion Industries, 2010b)

Motion Industries served industrial customers with MRO replacement parts and services. Motion's mission was "to meet or exceed our customers' needs in a timely manner by providing quality products and continuously improving our internal operations and the services we provide."[58] The company offered service to its customers 24/7/365. Those services included product delivery, repair and fabrication, assistance with quality processes, inventory management and logistics, and storeroom and replenishment tracking.[59]

At each of its locations, MI stocked significant amounts of inventory to meet quickly the product needs of its customers in the area. Manufacturing trends and government policies had led to opportunities in the "green" and energy-efficient product markets; MI offered energy-efficient motors and drives and recyclable parts and supplies. The company had return privileges with most of its suppliers, which protected it from inventory obsolescence. It also had ongoing purchase agreements with existing customers adding up to about 40 percent of annual sales volume.

Motion Industries grew through strategic acquisitions. In 2008, it acquired Drago Supply Company, which had eight locations in Texas, Arkansas, and Louisiana. Motion retained Drago family members as the management team for these locations, which also kept the Drago name.[60] In December 2009, parent company GPC announced the pending acquisition of a $170 million business to expand industrial operations in Western Canada and the northwestern US. Acquisitions remained an integral part of MI's growth strategy, and its managers anticipated future acquisition opportunities.[61]

Concerns of Loftin's Managers

In early 2010, Loftin's managers were pondering the following issues:

1. The industrial distribution industry as a whole, including Loftin, had experienced a sharp decline in sales and profits as a result of the deep recession in 2008 and 2009. What could the company do to reduce its vulnerability to future economic downturns?

2. How should the company manage its growth strategy? Where and how should it seek to grow?

3. The company's goal was to increase sales to around $300 million within a two to three year period. If it achieved this goal, what would it need to do to maintain the Loftin culture and maintain consistency in its operations?

ENDNOTES

[1] The names of the company and its president have been disguised in this case; however, all other information about the company is true and correct.

[2] Industrial distributors included companies that sold a wide range of products and services, such as plumbing, electrical, heating and air conditioning parts and supplies, safety supplies, and materials handling equipment. Many distributors sold products from several different segments of the industry, and some had expanded their product lines in recent years. This case focuses on companies that sold bearings, power distribution and similar products, and related services. Appendix 1 contains information about the ten largest industrial distributors in the world. Note that two of the ten companies, Motion Industries and Applied Industrial Technologies, were competitors of Loftin.

[3] B. Loftin, interview, March 4, 2010.

[4] Southwest Case Research Association, (2010). Southwest Case Research Association Case Writing Competition. Dallas, Texas, March 4, 2010.

[5] B. Loftin, interview, March 4, 2010.

[6] C. Barker, interview, March 4, 2010.

[7] C. Barker, interview, March 4, 2010.

[8] B. Loftin, interview, March 4, 2010.

[9] B. Loftin, interview, March 4, 2010.

[10] Southwest Case Research Association, (2010).

[11] B. Loftin, interview, March 4, 2010.

[12] Southwest Case Research Association, (2010).

[13] B. Loftin, interview, March 4, 2010.

[14] B. Loftin, interview, March 4, 2010.

[15] S. Mikkelsen, interview, March 4, 2010.

[16] S. Mikkelsen, interview, March 4, 2010.

[17] C. Barker, interview, March 4, 2010.

[18] S. Mikkelsen, interview, March 4, 2010.

[19] B. Loftin, interview, March 4, 2010.

[20] B. Loftin, interview, March 4, 2010.

[21] Avery, Susan (2009). All's Well, If the Price is Right. *Industrial Distribution*, July/August, 2009, 34-37.

[22] C. Barker, interview, March 4, 2010.

[23] B. Loftin, interview, March 4, 2010.

[24] B. Loftin, interview, March 4, 2010.

[25] Keough, Jack (2009a). Fighting back against a deep recession. *Industrial Distribution*. July/August 2009, 26-29.

[26] Keough, Jack (2009b). The problems facing distribution. *Industrial Distribution*. July/August 2009, 7.

[27] Kickham, Victoria Fraza (2009b). Staying Independent. *Industrial Distribution*. May/June 2009, 44-47.

[28] Keough, Jack (2009c). Technology takes on new importance. *Industrial Distribution*. November/December 2009, 14-16.

[29] B. Loftin, interview, March 4, 2010.

[30] C. Barker, interview, March 4, 2010.

[31] B. Moran, interview, March 4, 2010.

[32] B. Loftin, interview, March 4, 2010.

[33] C. Barker, interview, March 4, 2010.

[34] S. Mikkelsen, interview, March 4, 2010.

[35] C. Barker, interview, March 4, 2010.

[36] B. Loftin, interview, March 4, 2010.

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Appendix 1
Top 10 Largest Industrial Distributors

Company Name: **Wolseley**	Ranking based on 2008 sales: 1 $33.1 billion	Headquarters: Reading, England	Locations: 5,000 concentrated in Europe and North America
Product Lines: Building materials, plumbing and heating supplies, construction supplies	Customers: Professional contractors	Growth Strategy: Diversify range of products and geographic locations; growth through acquisitions	
Company Name: **The Wurth Group of North America**	Ranking based on 2008 sales: 2 $12.4 billion	Headquarters: Kunzelsau, Germany	Locations: 86 countries
Product Lines: Fastener and assembly components	Customers: Automotive, woodworking, metal working, construction	Growth Strategy: Maintain capital (company is privately held) and position for growth once the recession ends	
Company Name: **HD Supply**	Ranking based on 2008 sales: 3 $9.8 billion	Headquarters: Atlanta, GA	Locations: 900 in US and Canada
Product Lines: Construction and industrial supplies for infrastructure, maintenance and repair. Operates in 10 related industry segments	Customers: Construction contractors, governments, manufacturers	Growth Strategy: Focus on generating cash flow growth; increase sales from private label brands; grow through acquisitions	
Company Name: **W.W. Grainger**	Ranking based on 2008 sales: 4 $6.9 billion	Headquarters: Lake Forest, IL	Locations: 620, primarily in US but also Canada, Mexico, China
Product Lines: Facilities maintenance and other MRO products	Customers: Factory maintenance departments, service shops, governments, retail stores, contractors	Growth Strategy: Offer a large inventory; sell primarily through catalogs, including a “green” catalog	

Company Name: **McJunkin-Red Man**	Ranking based on 2008 sales: 5 $5.2 billion	Headquarters: Tulsa, OK and Charleston, WV	Locations: 250+
Product Lines: Pipes, valves, fittings	Customers: Oil and gas industry	Growth Strategy: Recently formed through merger of McJunkin and Red Man. Seeks continued growth through acquisitions	
Company Name: **Airgas**	Ranking based on 2008 sales: 6 $2.7 billion	Headquarters: Radnor, PA	Locations: 1,100+ in US and Canada
Product Lines: Industrial, medical, and specialty gases and related products	Customers: Health care providers, manufactures that use gases and welding supplies	Growth Strategy: Growth through acquisitions; using down time associated with recession to find ways to control costs	
Company Name: **Motion Industries**	Ranking based on 2008 sales: 7 $3.5 billion	Headquarters: Birmingham, AL	Locations: 518
Product Lines: Bearings, power transmission and fluid power products, hose and accessories	Customers: Food processing, mining, automotive, petrochemical, forest products, paper, pharmaceutical, power generation, wastewater management, wind and solar power	Growth Strategy: Sell additional products to existing customers; maintain active acquisition schedule, especially in industrial automation	
Company Name: **Wilson Industries**	Ranking based on 2008 sales: 8 $2.7 billion	Headquarters: Houston, TX	Locations: 250
Product Lines: Welding supplies, welding curtains, safety supplies	Customers: oil industry, automotive, electronics, laser industry, general manufacturing, construction, material handling, warehousing, safety, utilities	Growth Strategy: Grow with the energy business (oil and gas, mining)	

Company Name: **Fastenal**	Ranking based on 2008 sales: 9 $2.3 billion	Headquarters: Winona, MN	Locations: 2,311
Product Lines: Nuts, bolts, other fasteners	Customers: Original equipment manufacturers, MRO customers, contractors	Growth Strategy: Pursue organic growth through opening new stores and expand product lines	
Company Name: **Applied Industrial Technologies**	Ranking based on 2008 sales: 10 $2.1 billion	Headquarters: Cleveland, OH	Locations: 474 in US, Canada, Mexico
Product Lines: Power transmission products, bearings, industrial rubber products, tools, safety supplies, general maintenance products	Customers: Agriculture and food processors, mining, automotive, utilities, governments	Growth Strategy: Offer wide range of products to customers; increase amount of sales made to governments; grow through acquisitions	

(Avery, 2009; Industrial Distribution, 2009; DataMonitor, 2007; DataMonitor 2009a; DataMonitor, 2009b, DataMonitor, 2009c, DataMonitor, 2010; Olsztynski, 2007)

Appendix 2
Financial Statements for Loftin Distribution
Condensed Income Statements

For Years Ended 12/31	2009	2008	2007
Revenues, net	$ 100,355,957	$ 122,253,475	$ 117,534,228
Cost of goods sold	68,666,757	82,619,072	79,815,443
Gross Profit	31,689,200	39,634,403	377,187,785
Selling and administrative expenses	25,204,330	24,891,218	23,291,220
Operating Income	6,484,870	14,743,185	14,427,565
Other revenues and expenses			
Other revenues	66,774	304,720	68,122
Interest expense	(26,793)	(28,073)	(154,431)
Net Income	$ 6,524,851	$ 15,019,833	$ 14,341,256

Balance Sheets

As of 12/31	2009	2008	2007
Assets			
Cash	$ 4,271,723	$ 1,374,674	$ 763,390
Accounts receivable	10,702,149	14,780,455	13,198,212
Inventory	23,483,785	26,315,348	20,890,168
Notes receivable	312,899	323,683	119,054
Total current assets	38,770,556	42,794,160	34,970,824
Fixed assets, net	12,637,996	11,153,517	9,277,307
Deposits	28,142	24,441	34,524
Intangibles	2,890,901	2,506,720	77,720
Total noncurrent assets	15,557,039	13,684,678	9,389,551
Total assets	$ 54,327,595	$ 56,478,838	$ 44,360,375

Liabilities and equity			
Current liabilities			
Accounts payable	$ 3,640,179	$ 5,063,743	$ 4,532,156
Cash overdraft*	0	99,144	149,471
Accrued expenses	1,381,140	1,988,432	1,511,698
Line of credit	0	3,295,502	1,547,126
Other payables	36,103	31,392	32,717
Total current liabilities	5,057,422	10,478,213	7,773,168
Noncurrent liabilities			
Notes payable to related party	247,932	322,290	391,787
Notes payable	150,000	40,000	251,685
Other	0	100,000	0
Total noncurrent liabilities	397,932	462,290	643,472
Partners' capital	48,872,241	45,538,335	35,943,735
Total liabilities and partners' capital	$ 54,327,595	$ 56,478,838	$ 44,360,375

*****Loftin had a line of credit with its bank. These bank overdrafts represented amounts of checks that Loftin had written but that had not yet reached its bank. When the checks did reach the bank, the bank covered the checks and added these amounts to Loftin's balance on the line of credit.

Statements of Cash Flows

For the years ended December 31	2009	2008	2007
Cash flows from operating activities			
Net income	$ 6,524,851	$ 15,019,833	$ 14,341,256
Add (deduct) noncash items			
Bad debt expense	206,568	91,114	119,529
Depreciation & amortization	1,058,390	955,002	844,809
Gain on sale of property	(31,496)	(217,333)	(60,715)
Cash provided by working capital components			
Accounts receivable	3,871,738	(1,016,133)	(995,760)
Inventories	2,831,563	(4,115,226)	(2,610,594)
Prepaid expenses, deposits, and other assets	7,084	(194,547)	6,935
Intangible assets	0	0	(1,000)
Accounts payable and overdraft	(1,423,564)	531,587	387,571
Accrued expenses	(602,581)	425,082	252,394
Net cash provided by operating activities	$ 12,442,553	$ 11,479,159	$ 12,284,425
Cash flows from investing activities			
Purchases of property, plant, and equipment	$ (2,592,607)	$ (3,054,757)	$ (2,474,535)
Proceeds from sale of assets	81,234	591,878	93,861
Cash used for business acquisitions	(383,181)	(4,446,958)	0
Net cash used in investing activities	$ (2,894,554)	$ (6,909,837)	$ (2,380,674)
Cash flows from financing activities			
Proceeds from notes payable and line of credit	$ 5,311,129	$ 6,489,670	$ 24,163,678
Repayments of notes payable and line of credit	(8,770,133)	(5,022,476)	(28,086,498)
Distributions to partners	(3,191,945)	(5,425,233)	(5,654,454)
Net cash used in financing activities	$ (6,650,949)	$ (3,958,039)	$ (9,577,274)

Net increase in cash	$ 2,897,050	$ 611,283	$ 326,477
Cash and cash equivalents, beginning of year	1,374,673	763,390	436,914
Cash and cash equivalents, end of year	$ 4,271,723	$ 1,374,673	$ 763,391

(Southwest Case Research Association, 2010)

Appendix 3
Financial Statements for Applied Industrial Technologies

(amounts in thousands except per-share amounts)

Statements of Consolidated Income			
Year Ended June 30,	**2009**	**2008**	**2007**
Net Sales	$1,923,148	$2,089,456	$ 2,014,109
Cost of Sales	1,403,138	1,520,173	1,466,057
Gross Margin	520,010	569,283	548,052
Selling, Distribution and Administrative	410,912	416,459	413,041
Goodwill Impairment	36,605		
Operating Income	72,493	152,824	135,011
Interest Expense	5,523	4,939	5,798
Interest Income	(1,099)	(4,057)	(3,438)
Other Expense (Income)	2,255	227	(1,179)
Net Other Income	6,679	1,109	1,181
Income Before Income Taxes	65,814	151,715	133,830
Income Tax Expense	23,554	56,259	47,808
Net Income	$ 42,260	$ 95,456	$ 86,022
Net Income Per Share – Basic	$1.00	$ 2.23	$ 1.97
Net Income Per Share - Diluted	$ 0.99	$ 2.19	$ 1.93

Consolidated Balance Sheet		
June 30,	**2009**	**2008**
Assets		
Current assets		
Cash and cash equivalents	$ 27,642	$ 101,830
Accounts receivable, net	198,792	245,119
Inventories	254,690	210,723
Other current assets	44,470	48,525
Total current assets	525,594	606,197
Property - net	62,735	64,997
Goodwill	63,108	64,685

Intangibles, net	95,832	19,164
Other assets	62,059	43,728
Total Assets	$ 809,328	$ 798,771
Liabilities		
Current liabilities		
Accounts payable	$ 80,655	$ 109,822
Short-term debt	5,000	
Compensation and related benefits	34,695	56,172
Other current liabilities	36,206	31,017
Total current liabilities	156,556	197,011
Long-term debt	75,000	25,000
Postemployment benefits	43,186	37,746
Other liabilities	26,484	36,939
Total Liabilities	301,226	296,696
Shareholders' Equity		
Preferred stock - no par value;		
2,500 shares authorized;		
none issued or outstanding		
Common stock - no par value;		
80,000 shares authorized;		
54,213 shares issued	10,000	10,000
Additional paid-in capital	136,895	133,078
Income retained for use in the business	560,574	543,692
Treasury shares - at cost		
(11,929 and 11,923 shares)	(191,518)	(190,944)
Accumulated other comprehensive		
income (loss)	(7,849)	6,249
Total Shareholders' Equity	508,102	502,075
Total Liab. & Shareholders' Equity	$ 809,328	$ 798,771

(Applied Industrial Technologies, 2009)

Appendix 4
DXP Enterprises, Inc. and Subsidiaries Financial Statements
Consolidated Statements of Operations
(In thousands except per share amounts)

	Years Ended December 31		
	2009	**2008**	**2007**
Sales	$583,226	$736,883	$444,547
Cost of sales	431,812	529,895	318,855
Gross profit	151,414	206,988	125,692
Selling, general and administrative expense	147,795	158,797	93,800
Goodwill and other intangible impairment	52,951	-	
Operating income (loss)	(49,332)	48,191	31,892
Other income	95	223	349
Interest expense	(5,245)	(6,130)	(3,344)
Income (loss) before provision for income taxes	(54,482)	42,284	28,897
Provision (benefit) for income taxes	(12,070)	16,397	11,550
Net income (loss)	(42,412)	25,887	17,347
Preferred stock dividend	(90)	(90)	(90)
Net income (loss) attributable to common stockholders	$(42,502)	$25,797	417,257
Per share and share amounts			
Basic earnings (loss) per share	$(3.24)	$1.99	$1.46
Common shares outstanding	13,117	12,945	11,811
Diluted earnings (loss) per share	$(3.24)	$1.87	$1.35
Common and common equivalent shares outstanding	13,117	13,869	12,860

Consolidated Balance Sheets

	December 31	
	2009	**2008**
Assets		
Current assets		
Cash	$2,344	$5,698
Trade accounts receivable, net	77,066	101,191
Inventories, net	72,581	119,097
Prepaid expenses and other current assets	3,533	2,851
Federal income tax recoverable	235	-

Deferred income taxes	7,833	3,863
Total current assets	163,592	232,700
Property and equipment, net	16,955	20,331
Goodwill	60,542	98,718
Other intangibles, net of accum. amortization	25,727	45,227
Noncurrent deferred income taxes	3,289	-
Other assets	822	880
Total assets	$270,927	$397,856
Liabilities and Shareholders' Equity		
Current liabilities		
Current portion of long-term debt	$12,595	$13,965
Trade accounts payable	51,185	57,551
Accrued wages and benefits	6,633	12,869
Customer advances	1,008	2,719
Federal income taxes payable	-	7,894
Other accrued liabilities	6,377	8,660
Total current liabilities	77,798	103,658
Long-term debt, less current portion	102,916	154,591
Deferred income taxes	-	9,419
Shareholders' equity		
Series A preferred stock	1	1
Series B convertible preferred stock	15	15
Common stock, $0.01 par value	129	128
Paid-in capital	58,037	56,206
Retained earnings	32,057	74,559
Accumulated other comprehensive income (loss)	(26)	(721)
Total shareholders' equity	90,213	130,188
Total liabilities and shareholders' equity	$270,927	$397,856

(DXP Enterprises, 2009)

Appendix 5

Financial Information for Kaman Industrial Technologies*

(amounts in thousands of dollars)

	2009	2008	2007
Net sales	$645,535	$776,970	$700,174
Operating income	12,612	35,397	33,038
Identifiable assets	203,845	229,460	195,518
Capital expenditures	3,139	4,216	2,650
Depreciation and amortization	3,536	3,096	2,507

(Kaman Corporation, 2009)

* Note that Kaman Industrial Technologies is part of Kaman Corporation, which prepares consolidated financial statements. This information is for Kaman Corporation's industrial distribution segment.

Appendix 6

Financial Information for Motion Industries

(amounts in thousands of dollars)*

	2009	2008	2007	2006	2005
Net sales	$2,885,782	$3,514,661	$3,350,954	$3,107,593	$2,795,699
Operating profit	162,353	294,652	281,762	257,022	214,222
Assets	865,431	1,025,292	969,666	910,734	976,903
Depreciation and amortization	7,611	7,632	8,565	7,941	8,345
Capital expenditures	2,987	7,575	8,340	6,187	5,695

(Genuine Parts Company, 2009)

* Note the Motion Industries is a subsidiary of Genuine Parts Company (GPC), which prepares consolidated financial statements including all of its operations in various industries. This appendix presents segment information for GPC's industrial distribution operation.