DRAFT

cc: N. T. Johnson
J. H. Davidson

INDUSTRIAL HYDRAULIC FLUIDS TRANSITION PLAN

T. L. Gossage

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The Situation

In the past, our major strength in the industrial hydraulic fluids business was our low cost chlorinated raw materials giving superior fire resistance to our fluids. These same materials had good solubility with oil and allowed us to formulate the Pydraul 312 series. The result was a very real and sizeable competitive advantage in terms of both quality and price over other synthetic fire resistant fluids.

That is all changed now. Polychlorinated biphenyls are out and polychlorinated terphenyls, in addition to being contaminated with PCBs, are also out. This leaves us with a line of resale water glycol fluids (available now) a straight phosphate ester (available shortly), and an oil-phosphate ester blend available late in the first quarter of 1972. In terms of cost and quality, none of these products will give us any significant advantage over our competitors. In addition, the changeover (the third in two years) will create an adverse affect, particularly on our major customers, the top 20 of which account for 60 % of our business.

top 5 top 10

This means that when the transition has been completed, we will be left with considerably less market share than we now have, with ill will at certain customers and potential accounts,

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and with no technical or cost advantage to regain our position. With these difficulties our sales growth in the future can not be as steep as our sales growth in the past, and our base will be less.

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Objective

Our objective in this transition program simply stated is to ~~accomplish the transition and~~ be out of PCB's/PCT's by July 1, 1972, and to salvage as large a share of the market as possible at a profit. We expect to keep at least 50% of our business, but We must take several steps as quickly as possible in order to achieve this.

General Motors

G. M. alone accounts for 18 % of our business. We must move immediately to convert G. M. to our phosphate ester fluid. ~~We have been told by~~ The Chevrolet Division, which is over half of the G. M. business and which will probably determine what all of G. M. does, (has told us) ~~that~~ they will drain and flush all PCB containing fluids from their machines and refill with a new product. We will try to sell them our phosphate ester fluid at list price and charge fully for incineration of the old fluid. If necessary to salvage the business, we will capitulate on incineration and give some price concession on initial fill. In return, we will ask for a three year supply period to recover our costs.

We will not sell a low price phosphate ester as a replacement

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for A200B. If General Motors goes to the phosphate ester and if we sell a low priced phosphate ester to one location, we will have to sell it to all of them. Due to the large share of our total business that G.M. represents, selling to them at a low price would undermine the profitability of our total Pydraul program. In addition, due to their size, it is possible that such a move would deteriorate the pricing of the phosphate esters at all accounts.

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Johnson Motors

Johnson Motors is in trouble with the State of Illinois because of too high phenolics discharge in their effluent. However, they appear to be sold on the wear low resistant synthetic fluid, which means phosphate esters, and all ~~synthetic~~ phosphate esters fluids will create phenolics in their effluent. We have gone to them and suggested they ~~also~~ move to our straight phosphate ester to avoid PCB problems and ~~to~~ that then solve their phenolics problem with treatment of their effluent. In terms of pricing and incineration, we will handle them in the same way as General Motors and, if necessary, make the same concessions.

Check Point

This should be a check point in our plan. If either General Motors or Johnson Motors are lost, we should re-evaluate our situation and decide again how best to proceed.

Selector I Accounts

After testing the water with General Motors and Johnson Motors and as soon as sufficient phosphate ester becomes available, we

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will move ~~immediately~~ to convert all Selector I accounts to straight phosphate esters.

Selector II Accounts

We will proceed at once ~~immediately~~ to develop, test and get Factory Mutual approval on a line of truly fire resistant oil/phosphate ester fluids. As soon as the development job is done and as soon as phosphate ester for these fluids becomes available, we will begin converting all Selector II accounts to these new products.

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Reclamation

We should move ~~immediately~~ now to work with Findett Service Co. on reclamation of the Pydraul fluids. This means quoting, in conjunction with Findett, for reclamation business wherever we can find it. Assuming this relationship is profitable, we will continue it and expand it to all places where we can be competitive. If it turns out that due to geography we cannot be competitive in conjunction with Findett in all locations, we will establish relationships with other reclaimers in those locales.

Capacity

Note that reclamation ultimately should have a substantial negative affect on our new fluid sales. This along with our loss of business during the transition must be taken into consideration when planning the capacity of our new phosphate ester plant.

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Vital 29 Type Fluids

Withdrawal of current Pydraul 312A type fluids from the market will force customers to go to either higher priced phosphate ester fluids, inferior quality water glycol fluids, or the Vital 29 type fluids which are not fire resistant after shear down of their polymer. To combat this we should go immediately to Factory Mutual, explain the situation on the fire resistance of these fluids and ask for Factory Mutual's position. If they remove their approval, that should essentially solve the problem. If not, we will develop a line of fluids in direct competition with Vital 29 and Dasco 300.

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Customer Notification

On April 15, 1971 I sent out a letter to the Pydraul mailing list saying: "There are now no PCBs in any of our Pydraul fluids." This letter is not true and has irritated the Chevrolet Division of General Motors and probably anyone else who knows that it is not true. We should write another letter immediately to the same list clearly stating that the letter was not true and giving them the facts on the PCB contamination. If possible, we can temper the letter with our plans for future fluids. However, getting the letter into our customers' hands before they get this information from our competitors should be our primary consideration.

Field Sales/Product Group Relationship

Major accounts where the Product Group may directly assist in

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conversion are listed in Appendix E. Current opinion is that all other accounts can be handled directly by the Field Salesmen(assuming we do have lower cost Selector II replacements).

To help prepare the salesmen for this transition, a meeting will be held in St. Louis ~~at~~ which will focus on strategic salesmen and their managers who will be in attendance. At ~~a minimum~~ the meeting we will lay out for them why we must transition, the reasons we will give the customer, replacement products with prices and benefits relative to our old products and competition, pollution aspects of PCBs, PCTs, and phosphate esters with a discussion of phenolics, B.O.D. and C.O.D., and oil contamination, and the legal aspects of our situation. We will leave them with a "Transition Handbook".

Also at this meeting we specifically define who will handle what accounts, the order in which they will be handled, and the timing on handling them.

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Advertising

To counter the negative affects of reformulation, we should plan and execute an advertising program that will explain why we are making this move and point out the advantages of our new fluids versus competition. Execution of this should begin ~~immediately.~~ now.

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Appendices

Attached are appendices which give some background on what our new Selector I and Selector II fluids will be along with their

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costs, prices and gross profit; what a typical conversion might cost us depending upon whether we get full price for the fluid and who pays for incineration; a list of our major customers; and what our profitability for 1972 may look like based on certain assumptions of conversion rates and costs of our new products.

C. L. Bradford

/pep

J. H. Davidson

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APPENDIX A

Proposed Pydraul Line and Pricing

Fluid	Pricing[1] T/T	T/L Drums	10-T/L Drums	5-9 Drums	1-4 Drums
Selector 1					
Pydraul 10 E	4.55	4.75	4.95	5.00	5.10
Pydraul 29 E-LT	3.60	3.80	4.00	4.05	4.15
Pydraul 30 E	Quote	3.65	3.75	3.80	3.85
Pydraul 50 E	Quote	3.65	3.75	3.80	3.85
Pydraul 65 E	Quote	~~3.65~~ 3.75	~~3.75~~ 3.85	~~3.80~~ 3.90	~~3.85~~ 3.95
Pydraul 95 E	Quote	3.85	3.95	4.00	4.05
Pydraul 115 E	Quote	3.95	4.05	4.10	4.15
Selector 2					
Pydraul 135 C	2.25	2.45	2.65	2.70	2.80
Pydraul 230 C	2.25	2.45	2.65	2.70	2.80
Pydraul 312 C	2.15	2.35	2.55	2.60	2.70
Pydraul 540 C	2.15	2.35	2.55	2.60	2.70

[1] 5 gallon can pricing - add .25/gallon to 1-4 drum price

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APPENDIX B

Pydraul Profitability

Fluid		Cost-Short Term[1] (Dixie CP)	Cost-Long Term[1] (Monsanto CP)	Gross S.P. (10-T/L Drums)	Long Term Gross Profit[2]
Selector 1					
lbs./gal.					
9.1	Pydraul 10 E	--	.191/lb	.545/lb	63%
9.4	Pydraul 29 E-LT	.222/lb	.215/lb	.425/lb	45%
9.9	Pydraul 30 E	.204/lb	.198/lb	.378/lb	43%
9.8	Pydraul 50 E	.227/lb	.213/lb	.383/lb	40%
9.7	Pydraul 65 E	.268/lb	.238/lb	~~.387/lb~~ .396	~~33%~~ 35%
9.7	Pydraul 95 E ?	.285/lb	.250/lb	.407/lb	34%
9.6	Pydraul 115 E	.295/lb	.256/lb	.422/lb	35%
Selector 2					
8.44	Pydraul 135 C	.170/lb	.165/lb	.314/lb	42%
8.44	Pydraul 230 C	.168/lb	.160/lb	.314/lb	44%
8.44	Pydraul 312 C	.170/lb	.160/lb	.302/lb	40%
8.49	Pydraul 540 C	.175/lb	.165/lb	.302/lb	38%

[1] Finished Product Cost Including Conversion and Drum Costs

[2] Average Freight and Warehousing at $.03/pound

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APPENDIX C

Pydraul Blends

All prices, costs and profit figures based on the following blends.

Pydraul 10 E

Pydraul 60

Pydraul 29 E-LT

N_2CP - 35%
S 141 - 63%
Polymer - 2%

Pydraul 30 E

N_2CP 40%
TPP 30%
CDP 30%

Pydraul 50 E

N_2CP 70%
TPP 30%

Pydraul 65 E

NCP 76%
TPP 24%

Pydraul 95 E ?

NCP 88%
TPP 12%

Pydraul 115 E

NCP 100%

Pydraul 135 C

N_2CP 20%
S 141 46%
*Oil 33+%
Polymer <1%

Pydraul 230 C

N_2CP 41%
S 141 16%
*Oil 42+%
Polymer <1%

Pydraul 312 C

N_2CP 46%
S 141 9%
*Oil 44+%
Polymer <1%

Pydraul 540 C

N_2CP 56%
*Oil 43+%
Polymer <1%

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*Oil could be Sunoco 800 N, Mobil 750 or H 230 but cost of all is $.04/pound

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APPENDIX D

Typical Customer Conversion

Customer Used for Calculations: Chevrolet - Bay City

Date for calculation of cost to customer and cost to Monsanto for conversion from Pydraul 312 A to Pydraul 65 E:

Machine Capacity = 50 machines x 300 gallons/machine = 15,000 gallons
Flushing fluid = 15,000 gallons petroleum oil
Freight Cost = $2.00/cwt. = $.22/gallon
Cost of Incineration = $.03/pound

Case 1

Chevy Bay City pays full price for new fluid plus flushing fluid plus freight for returned fluid plus $.03/pound to incinerate returned fluid.

A. Cost to Chevy

1.	15,000 gallons Pydraul 65 E @ $3.45/gallon	= $51,175
2.	15,000 gallons oil flushing fluid @ $.50/gallon	= 7,500
3.	15,000 gallons (138,000 lbs.) 312 A plus 15,000 gallons (112,000 lbs.) oil incineration @ $.03/pound	= 7,500
4.	Freight on returned fluid: 250,000 lbs. x .02/pound	= 5,000
	TOTAL Cost	= $71,175
	Cost per Gallon of new fluid (Does not include labor or downtime)	= $4.74/gallon

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(Case I Con't)

B. Gross Profit to Monsanto

Sales: 15,000 gallons @ $3.45/gallon	= $51,175
COGS: 138,000 pounds x .223/pound	= 30,774
	$20,401
Freight: 146,000 pounds x .02/pound	= 2,920
Gross Profit	= $17,581

$$\% \text{ Gross Profit} = \frac{17,581}{51,175 - 2,920} = 36.4\%$$

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Case II

Chevy - Bay City pays full price for new fluid plus flushing fluid but Monsanto pays for incineration cost and freight.

A. Cost to Chevy

15,000 gallons Pydraul 65 E @ $3.45/gallon	= $51,175
15,000 gallons oil flushing fluid @ $.50/gallon	= 7,500
TOTAL Cost	= $58,675
Cost per gallon new fluid (Does not include labor or downtime)	= $3.92/gallon

B. Gross Profit to Monsanto

Gross Sales		= $51,175
Less: COGS	$30,774	
Freight (New Fluid)	2,920	
Incineration Cost	7,500	
Freight (Returned Fluid)	5,000	= $46,194

$$\% \text{ Gross Profit} = \frac{4,981}{51,175 - 2920} = 10.3\%$$

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Case III

Chevy-Bay City pays full price for fluid but Monsanto pays for flushing fluid plus incineration costs and freight

A. Cost to Chevy

15,000 gallons Pydraul 65 E	= $51,175
Cost per gallon new Fluid (Does not include labor or downtime)	= $3.45/gallon

B. Gross Profit to Monsanto

Gross Sales			= $51,175
Less:	COGS	30,774	
	Freight(New Fluid)	2,920	
	Flushing Fluid	7,500	
	Incineration Cost	7,500	
	Freight (Returned Fluid)	5,000	= 53,694
		Net Loss	= $2,519

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APPENDIX F

1972 Financial Results

Case 1

1972 Financial results as currently budgeted:

Product	(ooo's lbs.) Volume	(ooo's $) Sales	(ooo's $) Gross Profit
Pydraul 60	45	22	9
Pydraul 150-A	1000	400	185
Pydraul A-200-B	—2300	621	171
Pydraul F-9-A	1150	380	148
Pydraul 625-A	275	83	24
Pydraul AC-A	600	192	67
Pydraul AC-A W.G.	24	7	--
Turbinol 153	325	107	36
Pydraul 135-A	1400	336	98
Pydraul 230-A	240	59	16
Pydraul 312-A	6850	1507	407
Pydraul 540-B	125	26	7
Total	14, 334	3740	1168
(Projected 1971 Results)	14, 267	4200	1300

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APPENDIX F

1972 Financial Results

Case II

1972 Financial results based on:

A. (1) Selector 1 fluids sold at 75% 1972 budget volume through 3/31/72

(2) NCP fluids replace Selector 1 fluids on 3/31/71 and sold at 50% 1972 budget volume from 3/31/72 through end of 1972

B. (1) Selector 2 fluids sold at 75% of 1972 budget volume through 6/30/72

(2) NCP/oil fluids replace Selector 2 fluids on 6/30/72 and sold at 50% 1972 budget volume from 6/30/72 through end of 1972.

C. General Motors plants on NCP from 1/1/72 - A-200-B to 50 E
- 312-A to 65 E

Product *	Volume (ooo's lbs)	Sales (ooo's $)	Gross Profit (ooo's $)
Selector 1			
Pydraul ~~60~~ 45 E	~~95~~	~~12~~ 22	~~3~~ 9
Pydraul 29 E-LT	560	222	101
Pydraul 30 E	193	63	31
Pydraul 50 E	1910	656	261
Pydraul 65 E	1225	437	147
Pydraul 95 E	340	128	43
Pydraul 115 E	152	59	18
Selector 2			
Pydraul 135 C	825	263	72
Pydraul 230-C	144	39	12
Pydraul 312 C	2800	689	221
Pydraul 540 C	72	17	5
TOTAL	~~8246~~ 8266	2585 2595	~~935~~ 920

* Financial results for new products includes results for old products as specified above.

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APPENDIX G

Incineration Costs

Gallons*	Incin. Cost @ $.03/pound	Freight @ .025/pound	Total
100,000	$28,800	$24,000	$52,800
150,000	43,200	36,000	79,200
200,000	57,600	48,000	105,600
250,000	72,000	60,000	132,000
300,000	86,400	72,000	158,400
400,000	115,200	96,000	211,200
500,000	144,000	120,000	264,000

*Average density of fluid @ 1.15 = 9.6 pounds/gallon

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