Operational Due Diligence Of Licensed Brands Household Goods Company: Uncovering Cost And Inventory Savings Opportunities And Assessing Operational Capabilities

The Challenge: A manufacturer of household cleaning and scented products under licensed brands was in exclusive negotiations to be acquired by a PE-owned consumer goods company. As part of Gotham's long-term relationship with the PE firm, we had previously assisted the consumer goods platform company in enhancing operations to prepare the company for add-on acquisitions. In light of Gotham's familiarity with the acquirer and the significant overlap in the two companies' customer base, the PE firm asked Gotham to quickly (in a week) assess the current operations and potential opportunities to reduce supply chain costs and inventory at the target both in terms of standalone improvements and synergies with the platform company.

The Partnership:
Analysis: A proprietary deal, there was no data room or centralized information. To build a solid fact base, Gotham conducted a 3-day site visit to gather readily available data, observe operations, and interview key managers. Armed with these facts and our supply chain expertise, the Gotham team quikly established a robust understanding of the business and its supply chain and hypothesized likely opportunity areas, including:

- Excessive inventories (including slow-moving and obsolete) that resulted from ad-hoc supply chain management processes (no MRP tools; reactive make-to-forecast system, with limited sourcing capabilities)
- Excess labor and material costs that were likely the result of an outdated and historically capital expenditure-constrained manufacturing facility and the absence of assembly process standards
- Rising freight and distribution costs that could likely be consolidated with the platform company given the overlap in customer base
- Excessive layers of supervision and other overhead.

After gaining agreement from the target management that these hypothesized opportunities were real, Gotham embarked on more robust analyses to pin down the scope of the opportunities. Gotham's key analytical activities covered:

- **Freight:** mode, lane, shipment characteristics, customer locations, carriers used, and discount rates in order to review potential consolidation options and calculate the likely cost structure and resulting savings
- **Inventory:** inventory turns profile, customer order and raw material lead times, and mapping of forecasting, planning, and purchasing processes. Based on observations from the site visit and comparison against benchmark inventory performance, the team concluded that a significant amount of slow moving and obsolete inventory (SLOB) existed at ScentCo. To further pin down the inventory situation, the team requested detailed SKU-level inventory and usage data. Team analysis of this detailed data confirmed and quantified preliminary results, and ScentCo's management team confirmed Gotham's conclusions

Potential Opportunities Translate Into An Estimated $2.9-$4.1MM In Operational Cost Savings And Pave The Way For Leveraging Synergies With The Parent Company
($MM)

Our several-day due diligence effort suggests that properly phasing a number of operations-related initiatives should deliver $2.9 to $4.1MM in savings

	Estimated Savings			
Initiative	**$MM**	**Primary Source(s)**	**Timing**	**Synergies With Parent Company**
1. Reduce outbound freight costs	$0.4-0.7	• Freight cost	Immediately	✓
2. Clean up forecasting/ planning/ purchasing process	$4.0-5.0 inventory reduction TBD material	• Inventory reduction; vendor renegotiation (also, enables China sourcing)	Immediately	✓
3. Establish material **4. standards and process controls** **5. Establish standards and tracking; tackle excess overhead**	$0.2-0.3 material $0.5-0.6 labor $0.2-0.3 O/H	• Direct labor cost (elimination of unnecessary data collection); overhead cost (right-size QC organization), material cost (SPC/SQC, elimination of overfill/waste) • Direct labor cost (correct staffing on the line); overhead cost (correct standards, removal of excess layers of supervision; modification of maintenance and changeover procedures)	Immediately Immediately	
6. Rationalize physical manufacturing assets	$1.6-2.2 O/H	• Elimination/additional outsourcing of operations; consolidation of remaining manufacturing in a central location	TBD	✓
7. Reconfigure distribution	TBD	• Consolidation of freight to common customers; potential consolidation of distribution into single, better-located DC	TBD	✓
Total	**$2.9-4.1 cost reductions** **$4.0-5.0 inventory reduction**			

Fully capturing these opportunities will require a strengthened management team and enhanced management control systems

- **Labor:** bridging from the previous year to budget and to current performance, including adjustments for volume and mix changes and improvements already underway. Combining this solid understanding of the current labor cost structure with the line uptime and productivity observations from the site visit, the Gotham team conducted an opportunity assessment, including an array of outsourcing/co-packer options and resulting cost structures
- **Material:** material waste levels (both in bills of material and appearing in variances). Observations during Gotham's site visits confirmed significant waste creation in the manufacturing facilities.

Gotham's due diligence effort also included an assessment of the target management team's functional leadership capabilities and controls.

Findings: Gotham created an opportunity assessment package for each cost bucket analyzed (standalone and synergistic perspective) and crafted a top-level plan to enable rapid, prioritized capture post-acquisition. Our efforts identified $3-4MM in cost reduction opportunities and $4-5MM in inventory reduction opportunities, including a significant amount in SLOB.

The Outcome: Our client successfully closed the acquisition and leveraged our findings on SLOB to get the seller to increase its inventory reserve. Since acquisition, Gotham assisted in capturing $4-5MM in inventory opportunities via planning improvement efforts, as well as aided in renegotiation of the merged companies' freight requirements, resulting in $2MM freight savings. the target continues to grow ($80MM in independent revenue), and the consolidated consumer products parent company (with one subsequent additional acquisition) is one of the largest suppliers to big-box retailers.

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