

Customer & Market Due Diligence Of Specialty Plastic Container Manufacturer: Valuing Market Potential Of An Add-On Acquisition

The Challenge: ContainerCo, a PE portfolio steel container manufacturer, was in exclusive negotiations to acquire PlastiCo, a specialty plastic container manufacturer for residential usage – a Gotham-identified target from our previous work with ContainerCo. To ensure proper valuation, ContainerCo asked Gotham to conduct a 2-week, robust customer and market due diligence of PlastiCo to gain a deep understanding of the dynamics of PlastiCo’s residential container niche and to pin down the growth potential of plastic containers in this niche.

The Partnership:

Analysis: In working with ContainerCo’s management team and the private equity team, Gotham structured the due diligence customer interview and market modeling effort to project the growth opportunity over the next 5 years from both current end-users of PlastiCo’s niche products and potential penetration in the user segment not using the product currently.

Gotham then created a thorough end-user questionnaire and a segmented, prioritized customer contact list based on size and geographic location. Our initial interview focus was on urban and large suburban market municipalities. Over the next week, Gotham interviewed 122 different end-users, representing 12% of PlastiCo’s total addressable market. Our interview with cities already converted (71 of 122) focused on: factors driving their decision to convert; their experience with PlastiCo’s products; ROI impact; and additional growth opportunities. Our interviews with cities not yet converted (51 of 122) focused on their plans, if any, for conversion and the factors affecting their decisions whether or not to convert. We also used the interview process to pin down key aspects of the customer’s purchasing behavior, the competitive dynamics, and perceived reputation and knowledge of PlastiCo, and any technology preferences.

While we were conducting our first round of interviews, Gotham built a market sizing model to understand the current addressable market size, current penetration rates, and potential market growth rates. To properly market size, our model incorporated housing unit growth rates by geographic area and city size, so that we could assign probability of conversion based on unique customer product requirements and replacement cycle.

Because our initial interviews and market sizing indicated that small customers represent a significant untapped opportunity, we conducted additional 24 interviews to get an understanding of small market dynamics.

Findings: Analysis of PlastiCo’s end market indicated that:

1. West region most penetrated with significant untapped penetration opportunities in Northeast
2. Very high rate of customer satisfaction; able to lower their costs as expected once initial hurdles were overcome
3. Key barriers to growth – high initial investment and lack of understanding on ROI
4. Extremely price-conscious customers that select lowest cost bid which meets specification
5. PlastiCo the perceived market leader in this niche.

Our detailed market sizing model indicated that the market is expected to grow at 3% CAGR over the next 5 years with penetration reaching 43-49% of the addressable market (vs. 33-37% currently), with the bulk of the growth opportunity likely in smaller communities where the penetration rates are still low. To achieve this level of penetration would require a proactive sales strategy focused on educating customers on benefits of this product, overcoming the high-cost perception, and easing the concerns about implementation challenges.

The Outcome: ContainerCo successfully acquired PlastiCo at an appropriate valuation that took into account our findings re: market size, growth potential, and customer perception. Since the deal closed, PlastiCo has been out-performing projections and doubled its EBITDA.

