

Operational Due Diligence Of Specialty Apparel Supplier: Developing Roadmap To Professionalize Operations And Support Aggressive Growth Plan

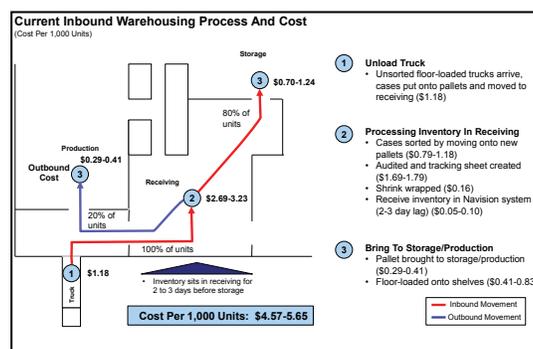
The Challenge: Our client, an operationally oriented PE firm, was acquiring an entrepreneurial private label supplier of fashion-driven specialty apparel. The target had achieved rapid sales growth from its successful entrance in an untapped market niche, a talented sales team, and a disciplined customer relationship management approach. While impressed by the company's solid front-end capabilities and growth opportunities, our client was concerned about the rudimentary state of the company's operations which was starting to affect service and drive rapidly growing inventory levels and warehouse costs. To establish the target's current operational performance and set the stage for improvements after deal closure, Gotham performed a 3-week operational due diligence effort, focused on warehouse, supply chain, and front-end operations.

Creation Of Supply Chain Roadmap To Gain A Head Start On Value Creation: As the target lacked virtually any cost or operational reporting, Gotham worked with the target's outsourced IT service provider to access 3 years of transaction-level data from the company's ERP system. Simultaneously, our team interviewed management and key operations personnel, mapped core processes, and observed warehouse operations. Leveraging this data and our qualitative findings, we built a robust fact base of the company's operational performance, including warehouse costs and capacity utilization, sales and SKU complexity, sourcing, inventory, and cost structure. We also built models to establish inventory opportunities and warehouse capacity/cost scenarios, and crafted an end-vision for supply chain, warehouse, KPIs, systems, and organization, and a 2-year value creation plan.

Warehouse Capacity Sufficient With \$1.3MM Cost Reduction Possible

To overcome the lack of warehouse information, Gotham spent 3 days in the warehouse mapping processes and material flow, timing every step, and measuring distances. The team determined the true warehouse capacity by measuring each warehouse room and simulating fully installed rack capacity, while taking into account safety and material flow constraints. Gotham found that current warehouse space was sufficient to support 3.7x current volume. The team also identified avoidable touches that were driving the operating costs unnecessarily higher. Gotham mapped out efficient processes and a new warehouse layout and material flow to minimize the number of touches and maximize capacity, with up to \$1.3MM savings per year, including:

- Optimizing inbound warehousing processes (freight unloading, receiving, and put away steps) via pre-sorting, flex conveyors, and pallet-loading, to reduce excess touches, **saving \$1.20-2.01 per 1,000 units**
- Reducing repetitive touches in the outbound warehousing process, **saving \$1.46-2.20 per 1,000 units**
- Moving the production area next to shipping to optimize material flow, **saving \$0.83-1.89 per 1,000 units in labor cost**
- Moving storage racks closer together and removing unnecessary walls to maximize capacity.



Formalized Supply Chain Processes Required To Meet Value Proposition, With An Opportunity To Reduce Inventory By 39%

Gotham's assessment confirmed the target's lack of supply chain processes. Inventory was managed at style level, not SKU level, creating confusion and significant rework when a style had to be repackaged for a different customer. Material transaction errors created situations where SKUs were not found when the order was picked, with the customer service team often having to go to the warehouse to establish stock availability. Planning entailed a 6-month running average even though the demand was seasonal. We also established statistical inventory targets at SKU level leading to a 39% inventory reduction opportunity from reducing excess inventory and disposing of obsolete inventory. To achieve supply chain process improvements and capture the inventory reduction opportunity, we detailed end-visions for:

- **Cross-Functional, Data-Driven Forecasting** process incorporating understanding of customer needs, seasonality, and trends
- **Systemized Inventory Planning And Management** with well-defined inventory strategies by type of SKU (e.g., SKUs sold to one customer vs. SKUs sold to several customers, SKUs that sold sporadically vs. sold every month) and targets, with inventory management at style-customer combination level to significantly reduce rework
- **Disciplined Purchasing/Inbound Logistics** process to create timely purchase orders, consolidate, track, and audit shipments
- **Streamlined Sales Order Entry And Management** with increased visibility to expected delivery date adherence
- **Accuracy/Visibility Of Inventory In System** ensuring all inventory transactions are properly accounted for via cycle counting.

Disciplined, Customer-Centric Front-End Operations Can Continue To Drive Rapid Growth

Robust conversations with the target's sales, marketing, and design team confirmed the effectiveness of the target's organized and professional sales approach. Gotham did raise several considerations to keep in mind moving forward – the need to reduce the strong reliance on a few key front-end people to avoid the risk of a growth bottleneck and/or loss of capability in the event of exit from the company and the need to “tweak” the specialty store oriented sales processes for department stores.

The Outcome: Gotham's operational due diligence effort confirmed our client's ongoing sense of the target's operations and provided a clear path forward to support the company's aggressive growth plans. Within a month of deal closure, management had reorganized the warehouse and started implementing other elements of our value creation plan.