Value Creation In Private Equity

Customer & Market Due Diligence Of Premium Home Appliance Manufacturer: Analyzing Retail Expansion Opportunities In Key States And Establishing Competitive Threats In Market Sub-Segment

The Challenge: Our client, a mid-market PE firm, was considering an investment in a leading manufacturer of premium home appliances. The target had carved out a niche at the highest end of the market, but its presence was limited to specialty appliance retailers in 2 geographic regions with over 90% of its revenue coming from just 4 states (NY, NJ, TX, and LA). Furthermore, mainstream market players were beginning to develop higher quality products, raising some concern about possible margin erosion in the future. Gotham was brought in to analyze the target's growth potential at retailers outside its core geographies; specifically, to assess and prioritize retailer penetration in five states (CA, MN, OH, TN, and NC) best suited for the target's premium product lines, identify key success factors for an expansion in these states, and evaluate the threat of other manufacturers entering the target's market niche.

Premium Home Appliance Expansion Study: To pin down the geographic, competitive, and retail channel dynamics of the target's premium home appliance market expansion, Gotham performed extensive primary research, interviewing 150+ store managers at local and regional specialty appliance retailers and distributors in the geographies of interest. In addition, our team developed a robust state-level fact base on overall demand for the target's appliance sub-segment, including data on usage/ shipments, consumer demographics, housing characteristics, and competitors utilizing government, industry, and company information and Gotham's proprietary database.

Of The 5 States Investigated, California And Minnesota Are Most Favorable For Geographic Expansion

Key success factors for premium specialty appliances in the target's sub-segment for the proposed expansion states were: high demand for these appliances, high household income, and prevalence of specialty appliance retailers. Of the 5 states, California and Minnesota had the most desired characteristics making them the most favorable markets for the target's expansion. In order to prioritize states, the Gotham team:

- 1. Performed an analytically-driven assessment of **premium appliance demand**, including appliance penetration, usage level, load hours, equipment age, as well as related data on weather patterns and housing age and mix.
- 2. Analyzed **household income** by distribution, median home prices, and rental rates, to determine states best matching target's consumer profiles.
- 3. Evaluated specialty retail channel dynamics for the concentration of appliance dealers/distributors, as well as for the penetration of big box retailers (indicator for lower probability for penetration) California and Minnesota had a lower-than-national average of big box stores (8.8 and 8.3 stores per MM people in CA and MN, respectively, versus a national average of 11.3 stores per MM people).

		Income	Channel Dynamics	Attractivenes
California	•	•	•	•
Minnesota	•	•	•	•
Ohio	•	•	0	0
Tennessee	0	O	O	O
North Carolina	•	O	0	O

Concerted Effort Required To Develop Premium Segment As Few Retailers Carry These Appliances

Regardless of the state, Gotham determined that expansion efforts will require a proactive approach to develop the premium market as few specialty appliance retailers carry products at target's premium price point. A comprehensive sample of specialty retailer interviews in the 5 states was conducted to determine the presence of regional appliance retail chains carrying premium appliances and of buying groups/distributors carrying premium products. On average in these 5 states, Gotham found only 11% of specialty retailers carried premium appliances in the target's segment while 67% carried premium brands in other appliance categories. The greatest prevalence of premium brands in other appliance categories were in California (88%) and Minnesota (83%), indicating a significant opportunity for target to capture share of wallet from these consumers. Gotham recommended translating target's premium offerings into a compelling strategy for these retailers, e.g., products that fit with retailers' high-service value proposition, opportunity for differentiation, and higher profit margins.

Negligible Threat From Competitors Entering Target's Sub-Segment Of Premium Home Appliance Market

For each state, including states where target was already present, Gotham assessed the competitive landscape (domestic and foreign appliance manufacturers) in the target's premium segment and found there to be no true competitors operating in these markets today – only one domestic player was perceived as having a premium offering, but did not match target's product lines in terms of features or price. And there was no indication that target would have to be concerned about protecting its existing business from any new foreign entrants – interviews with specialty retailers revealed only 1 mention (of 31 respondents) of a foreign entrant making inroads just below the target's premium segment.

The Outcome: Gotham's customer & market due diligence findings were a key input as our private equity client moved forward and successfully closed the transaction. Post-transaction close, the target immediately launched expansion initiatives in both California and Minnesota, utilizing Gotham's findings as a playbook for its geographic expansion strategy.