



The Dbriefs Private Companies series presents:

The Performance Imperative: Reaching Beyond Cost Cuts and Product Delivery Improvements

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January 30, 2013

Agenda

Middle market pressure

Obstacles and challenges

Getting real

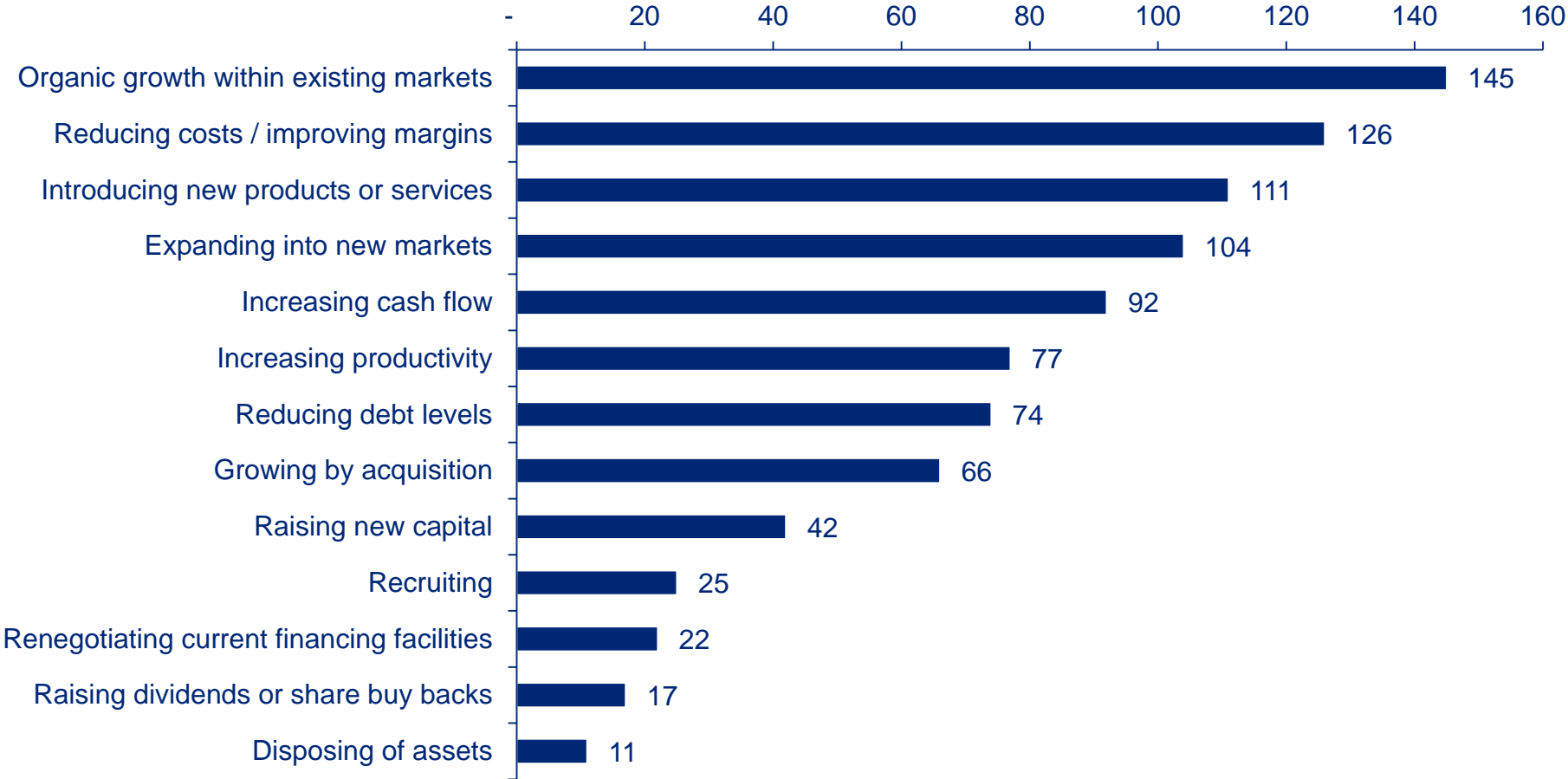
Question and answer

Poll question #1

What are your business priorities for 2013?

- Mergers and acquisitions
- Top line growth
- Increase productivity
- Reduce costs
- Raise capital
- Don't know/not applicable

Top priorities from a 2012 Deloitte study



Source: Deloitte Mid-market perspectives – 2012 report on America’s economic engine.

Score indicates relative mindshare .

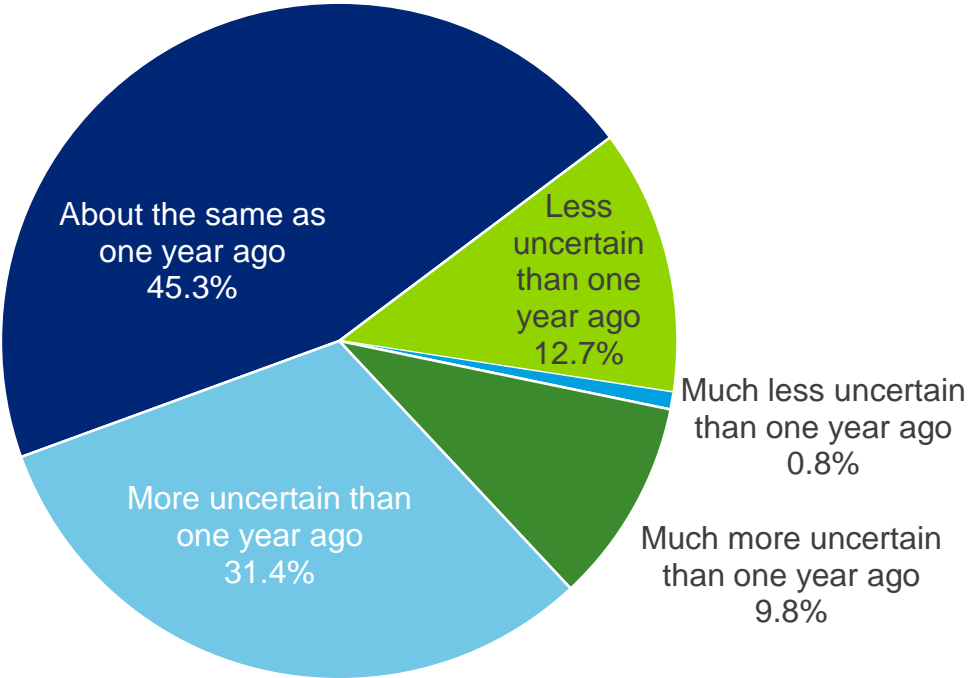
Middle market pressure

Current situation

- Middle market companies have unique challenges that constrain their ability to grow and provide returns for stakeholders.
 - Uncertainty around external factors including general economic growth, regulatory environment, taxes.
 - Growth strategies are constrained by resources – both human and capital.
 - Costs are difficult to reduce due to years of little economic growth, commodity prices and limited scale.
 - Talent is difficult to attract despite high unemployment.

The level of uncertainty is generally not improving

Compared to one year ago, the level of uncertainty in terms of factors that drive future business prospects



Source: Deloitte Mid-market perspectives – 2012 report on America’s economic engine

What to do?

- Middle market companies need to be more focused in order to leverage their smaller size and/or be more change-nimble to:
 - Allow fast response to external factors.
 - Maximize value from scarce resources.
 - Implement targeted process improvements and cost reductions.
 - Help create an engaged and committed work force.

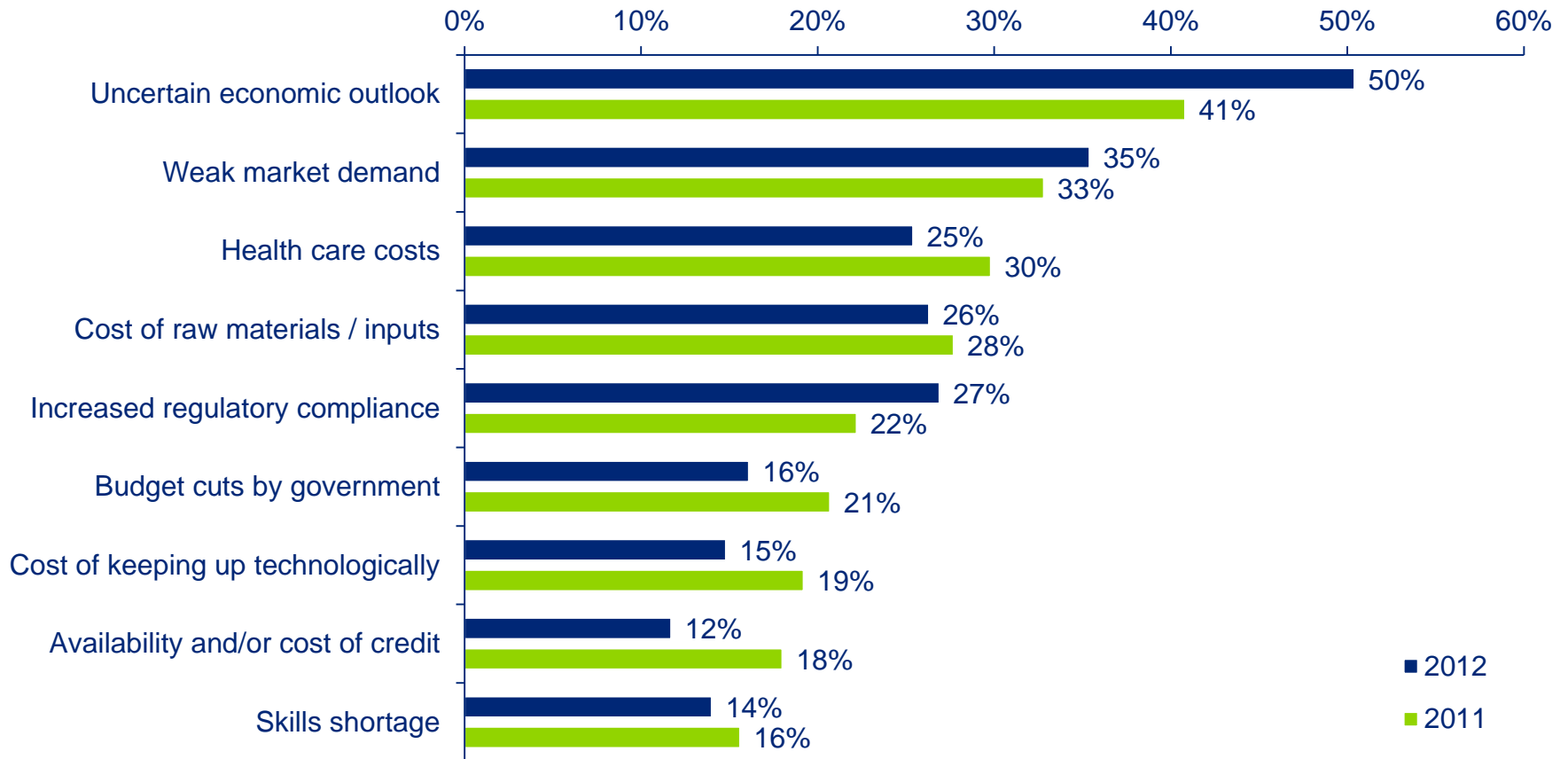
Obstacles and challenges

Poll question #2

What is the single biggest obstacle to increasing your companies' performance?

- Strategic direction
- Value creation
- Human resource constraints
- Competitors
- Capital constraints
- Don't know/not applicable

Biggest external obstacles from 2012 survey



Source: Deloitte Mid-market perspectives – 2012 report on America's economic engine

Challenges are often met with sub-optimal solutions

Challenges	Common responses
How and where to grow through new products, services and markets?	Overload the organization with growth initiatives. Examples include, launching too many product development projects, spreading sales and marketing resources across too many, or not the right, target markets.
How to reduce costs when constrained by lack of scale and buying power?	Blanket cost reductions without focus on process efficiency or key operational levers, and often overlooked opportunities (product complexity, insurance, working capital management).
How to attract and retain talent?	Hiring from outside the organization for key leadership positions rather than focusing on training and development.
How to access capital for growth?	Lack of credit / cost of credit causes working capital lines to fund operating losses or longer term investments.

These can create a number of unintended negative consequences...

Potential consequences

Challenges

How and where to grow through new products, services and markets?

Common responses

Overload the organization with growth initiatives. Examples include, launching too many product development projects, spreading sales and marketing resources across too many or not the right target markets.

Negative impacts of typical responses

- The organization's focus on core competencies (products and services) is diluted, possibly impacting quality and market share.
- Product / service development cycle times extend.
- Engineering and development resources stretched thin and stressed.
- Products and services are late to market or rushed to market with manufacturability, serviceability and quality issues.
- Markets, especially international, are entered without the organization, or the business processes, being ready which creates inefficiency and chaos, and possibly having to abandon the market.
- Lower margins from customer penalties.
- Loss of reputation and customers.

Potential consequences

Challenges

How to reduce costs when constrained by lack of scale and buying power?

Common responses

Blanket cost reductions without focus on process efficiency, key operational levers and often overlooked opportunities (product complexity, insurance, working capital management).

Negative impacts

- Tougher HR decisions are avoided and organization weakens as talent leaves.
- Leadership credibility questioned, and open communication to management declines
- Culture is impacted and morale declines causing a productivity decrease
- Processes remain inefficient and ineffective, with fewer resources to operate them.
- Lower procurement costs may come from higher minimum buys which increase inventory levels.
- Certain departments are viewed as less important by management and may bear the brunt of cost reductions.

Potential consequences

Challenges

How to access capital for growth?

Common responses

Selling strategic assets or reduce capital investment.

Using working capital lines to fund operating losses or longer term investments.

Negative impacts

- Hurts long-term growth potential.
- Build up of financial pressure and impacts across organization.
- Vicious cycle of dwindling liquidity.
- Selling assets below book value reduces earnings.
- Shrinking borrowing base availability is a “red flag” to lenders.

Potential consequences

Challenges

How to attract and retain talent?

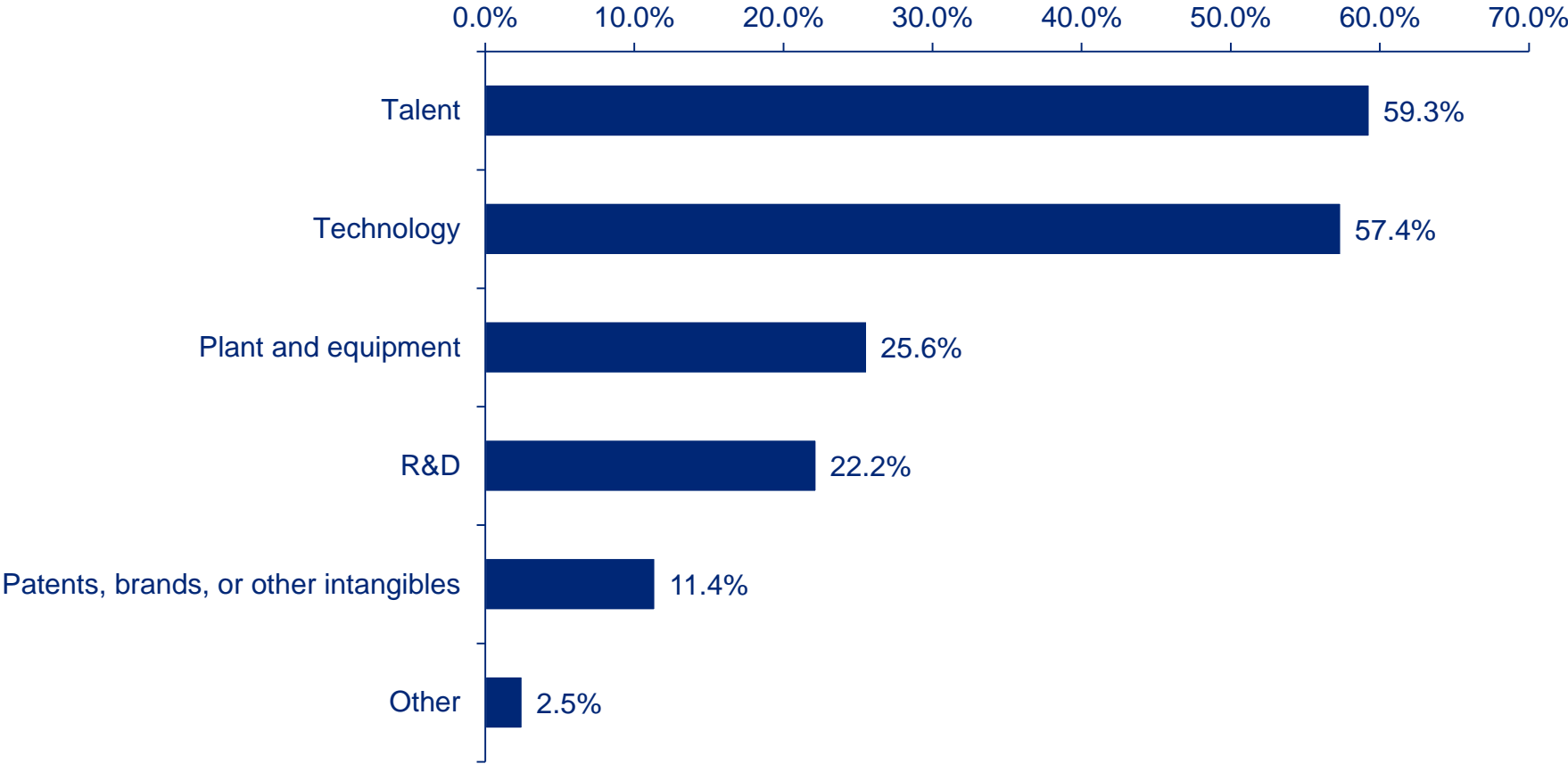
Common responses

Hiring from outside the organization for key leadership positions rather than focusing on training and development.

Negative impacts

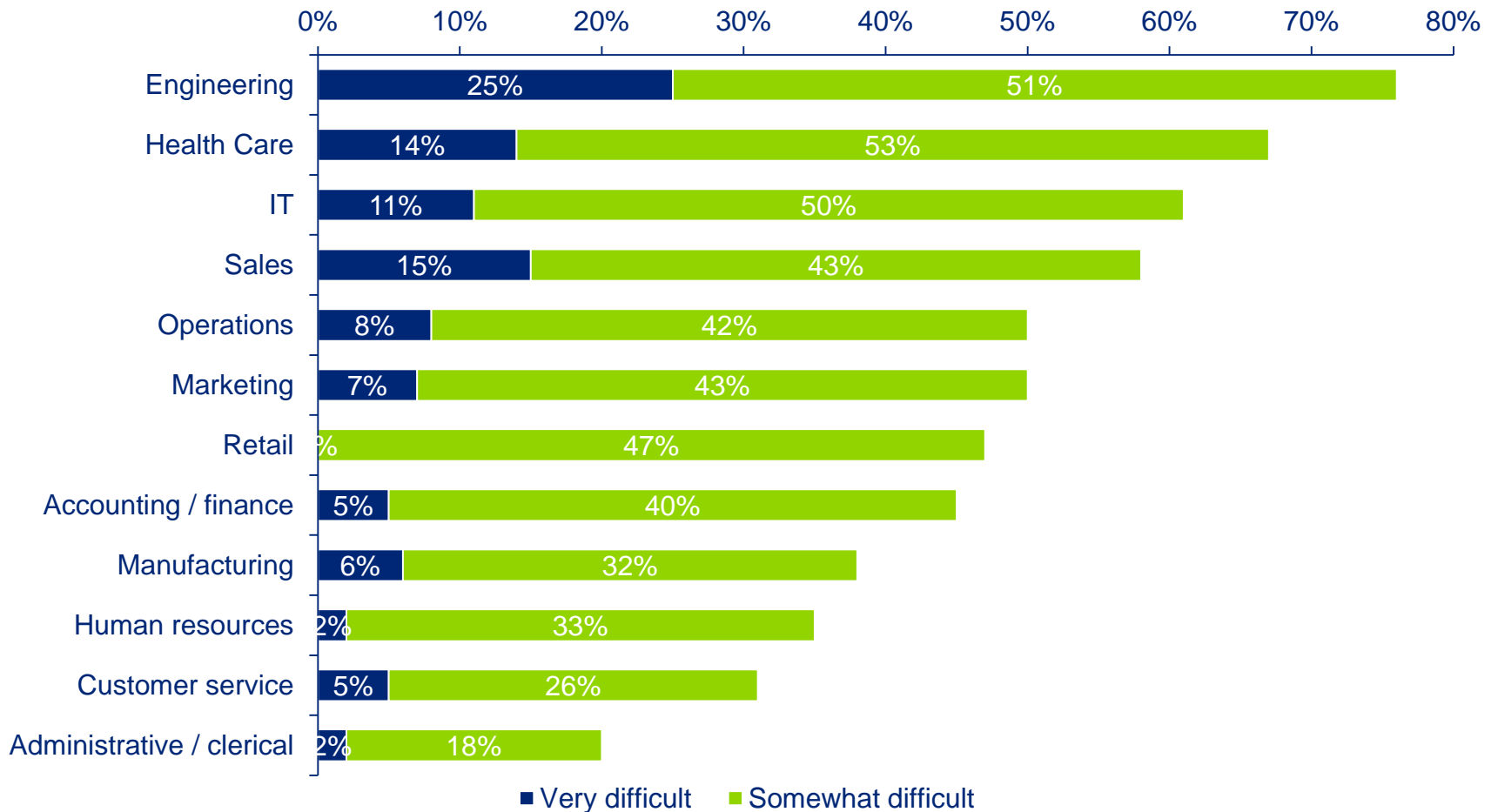
- Learning curve for new employees take focus away from other priorities
- Employees don't feel valued
- Morale declines and demotivated employees don't pursue advancement.
- Organizational turnover.
- Destructive organizational dynamics resulting in lower team efficiency and effectiveness, impacting productivity

Which internal investments offer the greatest potential for increasing productivity?



Source: Deloitte Mid-market perspectives – 2012 report on America’s economic engine

How difficult is it to find qualified candidates?



Source: Deloitte Mid-market perspectives – 2012 report on America's economic engine

Getting real

Appliance manufacturer– Case study

Appliance manufacturer

Privately owned international manufacturer of high-end kitchen appliances.

Situation

- Loss of revenue and profitability related to collapse of the housing market in 2007
- Increased product offerings resulting in greater complexity in engineering & manufacturing, lower inventory turns
- Inconsistent processes with regard to new product design and development resulting in longer product development cycle times
- Lower quality in certain product lines relative to strong brand perception resulting in higher than average service costs
- Poorly evolved processes and inconsistent interactions across the service process
- Needed help with project assessment and prioritization

Actions

- Led a team of Company managers to develop, prioritize and execute multiple improvement projects including:
- Reduced raw and finished goods inventory to generate cash
- Streamlined overhead processes to cut costs and improve EBITDA
- Overhauled outbound logistics to reduce freight costs, improve performance
- Redesigned products to take out cost and boost product margins
- Created new integrated product development process to streamline new product launches
- Redesign of customer service process to improve customer experience, reduce costs

Results

- Prevented significant near term liquidity issue
- Annual EBITDA doubled
- Established new discipline in initiative management to maximize results in shortest time

Newspaper publishing group – Case study

News publishing group

A family-owned newspaper and magazine publishing group. Owns 14 dailies and 30 weekly titles

Situation

- Transition issues from Print Centric to Multi-Media, Multi-Platform business model
- Faced with declining revenues from traditional advertising, Publisher needed to reduce its cost base, develop new revenue streams and expand its online presence.
- Had developed a 'Digital First' Strategy
- Focus of the review was six dailies and associated weekly titles in Southeastern U.S.

Actions

- Five-week operational analysis across editorial and advertising departments.
- Comprehensive benchmarking of all editorial departments across six daily newspapers to establish the current cost of quality, and the opportunities to reduce costs through excess capacity and changing the way they worked.
- Business process improvement effort to identify and eliminate organizational productivity constraints.
- Complete effectiveness review of print advertising sales force to identify non-value-added activities to eliminate in favor of supporting the online operation.
- Segmentation analysis of low-value accounts to focus on reducing the transaction cost of sales.

Results

- Identified editorial staff reductions of 31% through combination of reduced capacity, integrated newsrooms and changing the way they worked
- Developed plan to centralize the editorial sports and features departments
- Developed plan to centralize editorial production
- Sales force effectiveness review created an additional 40% capacity through transferring low-value accounts to a telephone sales operation and eliminating non-value-added activities.
- Have developed implementation program to realize the benefit run-rate within a 90-day period

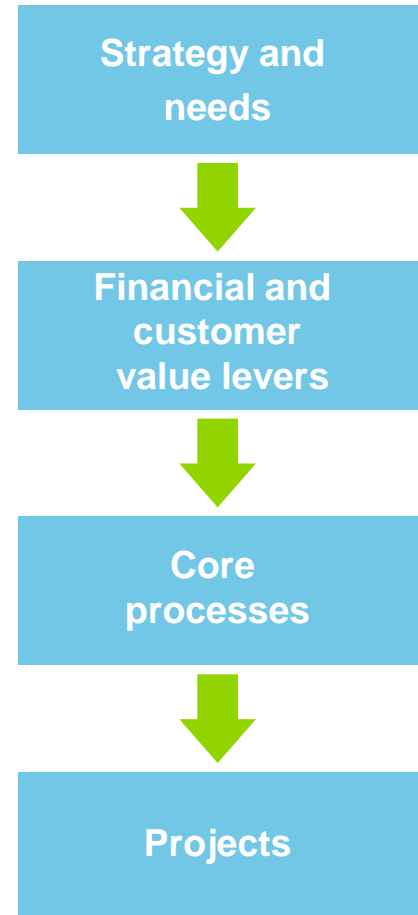
Poll question #3

What have been your frustrations with improvement initiatives?

- Speed to completion
- Robustness of solutions
- Depth of financial results
- Organizational momentum
- Lost opportunities
- Don't know/not applicable

Linking business needs to projects is critical

- Projects must support business strategy and needs.
- Financial and customer value levers link strategy to value creation potential (e.g. point you to the \$\$).
- Core processes link customer satisfaction to value levers. Processes are:
 - Where the work gets done
 - What drives cost
 - What customers see in your business
- Projects should be selected with the following fundamentals:
 - Properly defined and scoped
 - Highest potential benefit relative to the resources required
 - Ability to staff with appropriately skilled and motivated team

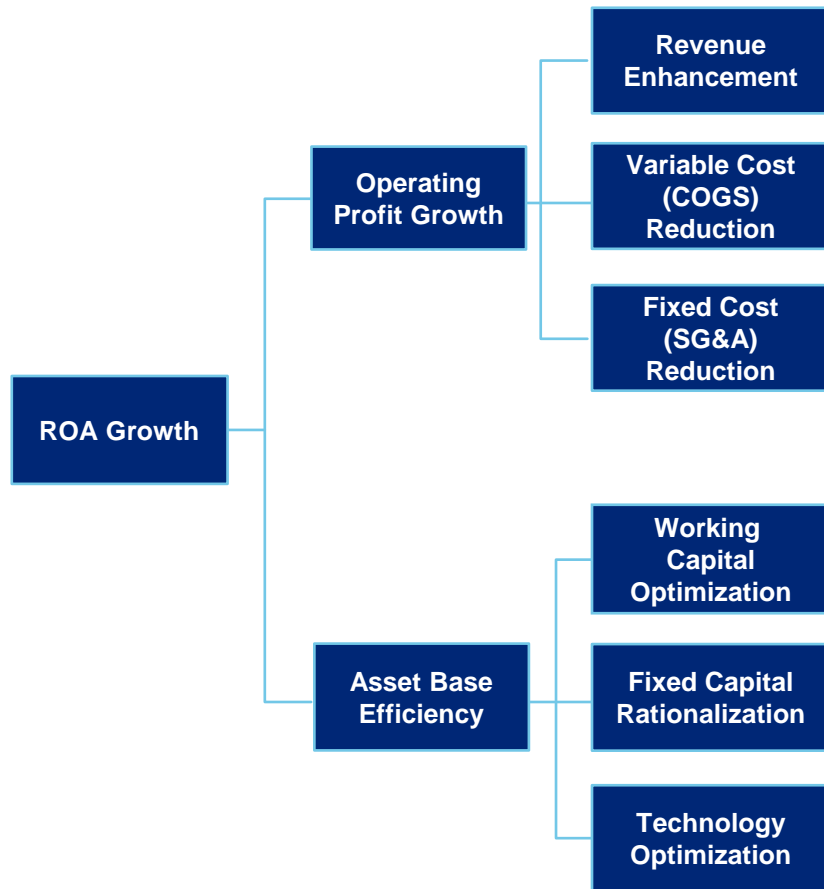


“It’s hard to be aggressive when you don’t know who to hit.”

— Vince Lombardi to a tackle who hadn’t learned the playbook

The middle market can leverage their smaller size and be more nimble than their larger competitors

Assess the operational drivers of financial results

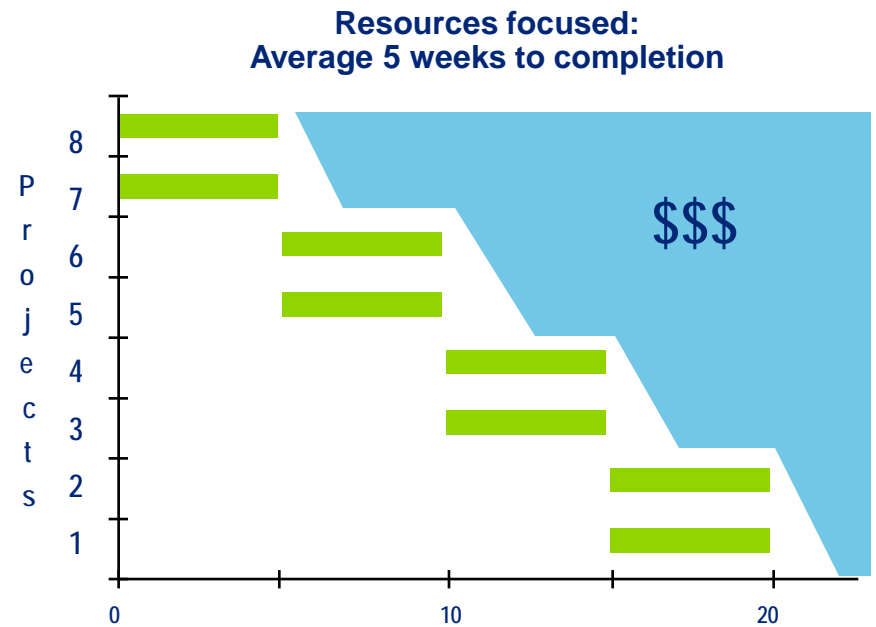
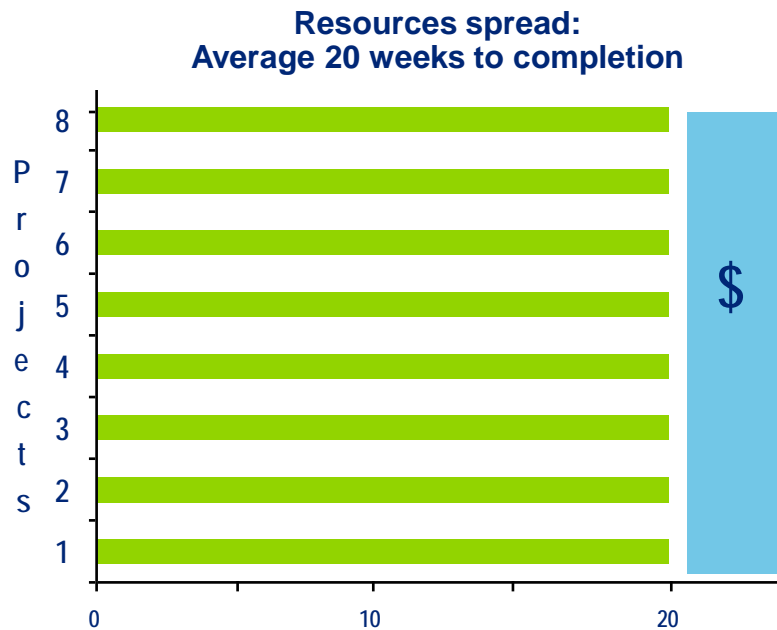


Examples

- Created strategic and market analysis, business plan, and implementation plan to roll up 3PLs into a \$1 billion Newco.
- Consolidated facilities and increased operating profit by over \$25 million in nine months for \$300 million cryogenic equipment manufacturer.
- Rationalized unprofitable programs (consolidated plants/eliminated costs associated with discontinued business) increasing EBITDA by \$4 million in one year for \$200 million motor components manufacturer.
- Improved on-time shipping from 50 to 90+% in six months for \$150 million commercial furniture manufacturer.
- Increased direct labor productivity by 20% in four months reducing monthly cash burn by \$600,000 for \$100 million point-of-purchase display manufacturer
- Increased inventory turns by 50% \$(5) million in nine months for \$40 million picture frame distributor
- Reconfigured the PeopleSoft ERP system for a \$400 million national Caribbean telecom monopoly

Focus resources on the priority projects and put others on "hold" – Just say "wait"

- Creates results faster
- Concentrates right resources on best projects
- Generates organizational momentum through results and personal success

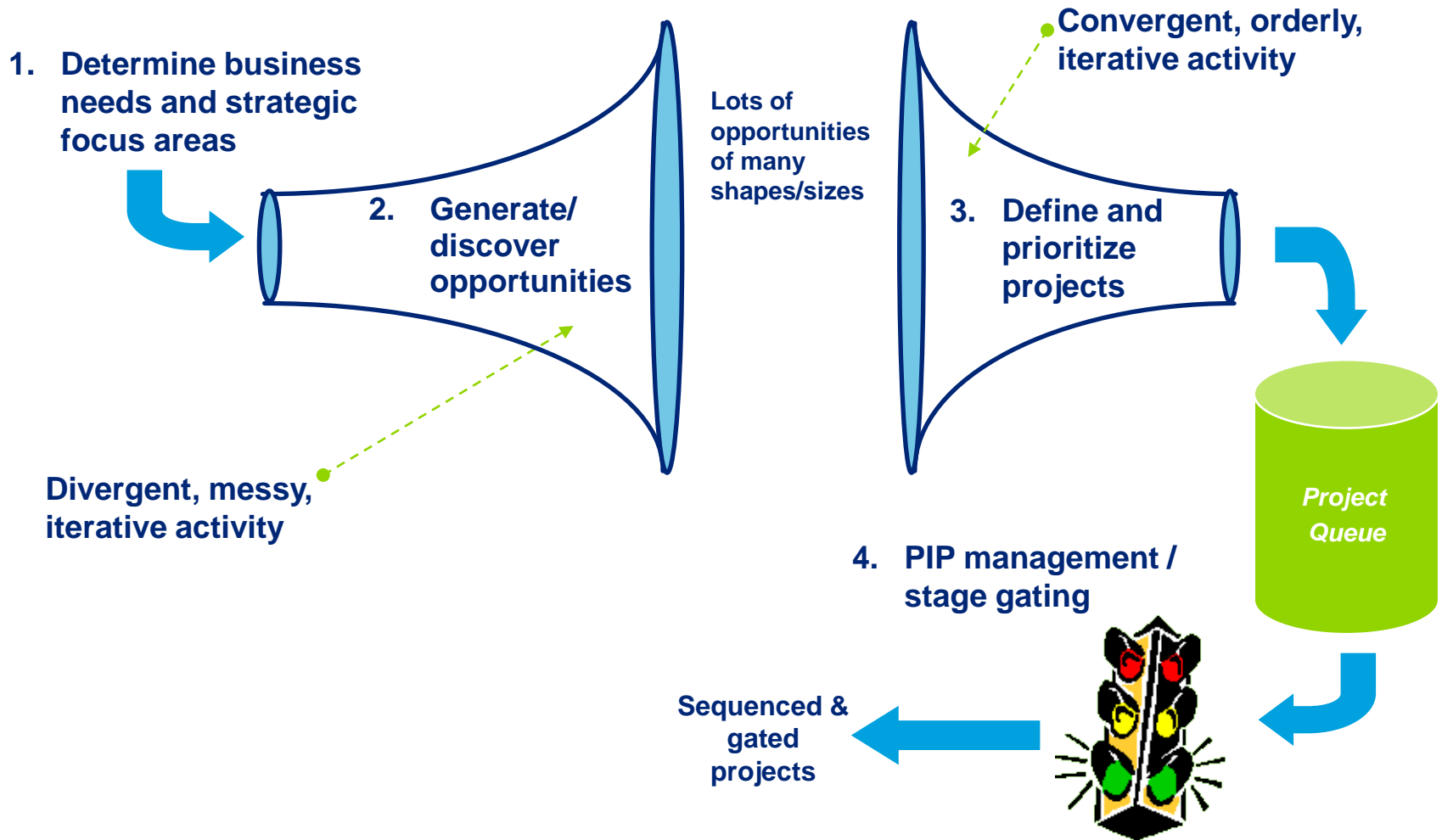


Poll question #4

How are projects selected in your organization?

- Leadership mandate
- Collaborative decision making
- “Squeaky wheel” selection
- Everyone does their own thing
- Don’t know/not applicable

How to identify, evaluate and prioritize projects

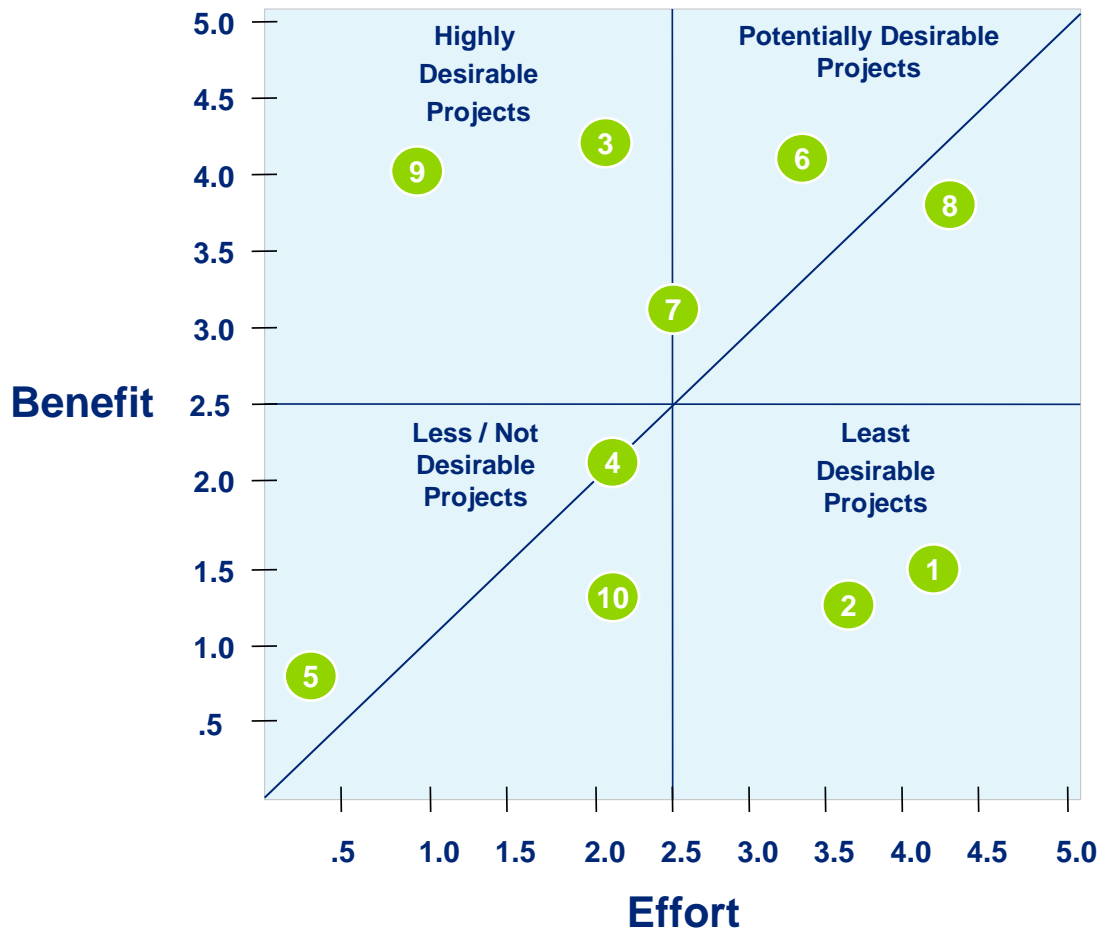


Projects are rated based on management defined criteria

PROJECT INFORMATION				IMPACT						EFFORT				
Project ID #	Manufacturing (M) or Business Process (BP)	Improvement Project (IP), Quick Hit (QH) or Other (O)	OPPORTUNITY/PROJECT DESCRIPTION	Strategic Fit	Revenue Growth	Cost Reduction	Capital Avoidance	Working Capital Reduction	TOTAL IMPACT	People Resources	Capital Resources	Duration of Project	Project Risk	TOTAL EFFORT
			<i>Variable Weightings</i>	0.20	0.20	0.20	0.20	0.20	1.00	0.25	0.25	0.25	0.25	1.00
1	M	IP	Project 1	1	0	3	1	1	1.2	1	0	1	1	0.8
2	M	QH	Project 2	3	1	5	3	3	3.0	0	0	1	3	1.0
3	M	O	Project 3	3	5	0	3	3	2.8	1	5	3	3	3.0
4	BP	IP	Project 4	5	0	3	3	3	2.8	1	1	0	0	0.5
5	M	QH	Project 5	3	1	0	1	1	1.2	3	5	1	0	2.3
6	BP	O	Project 6	3	0	3	3	3	2.4	3	1	5	3	3.0
7	BP	IP	Project 7	1	0	3	3	1	1.6	3	3	3	3	3.0
8	M	QH	Project 8	1	5	0	3	1	2.0	1	1	3	3	2.0
9	BP	O	Project 9	1	0	3	1	1	1.2	1	3	1	3	2.0
10	BP	IP	Project 10	5	1	0	0	1	1.4	1	3	1	3	2.0
11	M	QH	Project 11	3	5	0	3	3	2.8	3	0	1	1	1.3

Each Project will have a Total IMPACT score and a Total EFFORT score. These two scores will be used to “plot” the projects on a matrix. The position of the projects on the matrix will help us determine which ones we work on first.

Management evaluates projects and determines “go” or “hold” status



Benefit / Effort decision making

Assume in the example plot to the left that we need to select the next 3 projects to assign to resources. Which 3 projects would you select?

One possible solution:

Project 9 would be the first choice based on extremely high impact potential versus relatively low effort required.

Project 3 would be the second choice. It has slightly higher impact potential and significantly less effort than projects 6 & 8.

Projects 6 and 7 are both desirable and while **Project 6** clearly has more impact potential, they both lie on the same slope line and thus are mathematically equal. We would consider “tie breaker” variables to make a final decision (*e.g.*, strategic fit).

Other observations:

Projects 5 is an excellent **Quick Hit** candidate.

Projects 4 and 8 both have potential – and merit further analysis to learn more. Either could move into a more desirable position.

Lessons learned from process

- Management involvement and alignment is critical.
- Projects must be aligned with business strategy and needs to get the required attention.
- Resource allocation must take into account all initiatives within the business.
- If management is uncertain about the approach, initial projects will tend to be disconnected from strategy, be of low value, and lack support.
- The trick is not just identifying projects, but identifying the best projects, and the search doesn't stop.
- Look for quick hits (low effort, moderate benefit projects) to generate momentum.
- Initial projects should be scoped to ensure a good chance at winning.
- Projects tend to spawn more projects. Project selection process should be revisited frequently to ensure proper priority.
- Don't be afraid to kill a project-in-process if it does not continue to meet standards for prioritization/selection.

Conclusions and key take aways

- Most middle-market challenges can be overcome with a proven methodical approach.
- You are not in it alone, as most middle-market companies are facing, or have faced, these challenges...leverage their lessons learned.
- It does not take a lot of money to be successful with this approach, but focused execution is the key to success.
- Everyone in the organization must be aligned on the approach, understand the goals and support the process.
- Manage initiatives with a disciplined approach and the right tools.

Question and answer

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