

How to Play Value Creation Catch Up

Dig Deeper to Unlock, Amplify, and Accelerate the Opportunity



The COVID crisis doesn't have to change your exit plans or extend your holding period. You can stick to your timeframe and still get the IRR you expect by following proven strategies for accelerating the path to value creation.



Key Takeaways:

- Even while operating in the midst of a global pandemic, private equity firms have ample opportunity to quickly capture an acceptable rate of return.
- To achieve maximum value in the allotted timeframe, pursue high impact/easy-to-implement value creation opportunities.
- When selecting projects, keep an open mind and be willing to consider less obvious opportunities, such as value added/value engineering (VA/VE) projects, that often generate significant returns in short order.
- To expedite implementation, put solution frameworks into place quickly, track progress, and leverage process rigor and technology where possible.

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In our recent article on [Rethinking Your Value Creation Playbook](#), we drew a line in the sand, purporting that PE-owned companies don't necessarily have to adjust targets or holding periods in response to COVID-19. Rather, they need to refigure where the value lies and then adjust their strategies for capturing that value accordingly.

In many cases, especially for companies with exit dates looming, PE firms also have to push down the pedal on value creation. Ideally, PE companies will want to find the sweet spot where high EBITDA impact intersects with a short timeframe in order to get to the finish line with the greatest possible value capture.

Four Ways to Accelerate Value Creation:

1. **Reprioritise projects using timeframe as a metric**
2. **Make high-impact/highly-challenging projects more doable**
3. **Reduce costs or functionally improve product manufacturing processes**
4. **Accelerate project execution**

A worldwide pandemic might feel like plenty of justification to chalk up the last several months to lost ground. But many of the PE firms we work with aren't able or willing to move their exit dates or accept a lower rate of return. Fortunately, it's possible to accelerate value capture by speeding up both the selection and execution of projects designed to create value and improve a portfolio company's performance. But there's no time to waste. Companies with exit dates on the horizon will need to act now to unlock, amplify, and accelerate their value creation opportunities.

1. REPRIORITISE PROJECTS USING TIMEFRAME AS A METRIC

An impact/difficulty matrix is one of the simplest and most effective tools for quickly selecting value creation priorities. It plots various operational excellence improvements, business process improvements, and improvement opportunities by using expected EBITDA impact on one axis and project difficulty level on the other. The purpose of this exercise is to quickly and clearly create line of sight into where the best rate of return lies and to help decision makers carefully consider the effort required for a particular project's success. Projects that fall into the upper left-hand quadrant, where the impact is high and the relative effort is low, are the best bets; those that fall further to the right-hand side may not be as feasible. However, it's worth exploring if there are simple steps you can take to reduce implementation hurdles for these high-impact projects.

When speed is of the essence, you can replot this chart using your exit timeline for the X axis, where the numbers 1 to 10 represent months to implement, for example. Even if you have more time in your holding period, reconfiguring your chart is worthwhile. For many portfolio companies, demand, supply, and internal capabilities have shifted significantly due to the pandemic, which has an effect on the expected impact, timeframe, and difficulty level for each potential value creation initiative. Indeed, projects that may have been classified as high-impact but difficult to execute six months ago may fall into an entirely different quadrant today. The key is to ensure that the matrix is as realistic as possible given current market conditions.

We recently helped a PE firm that was looking to sell a portfolio company within 12 months to view its value creation opportunities based on the number of months it would take to complete (See Figure 1). Any projects requiring more than nine or 10 months to implement were left off the matrix. With this tool, the operating partners were able to instantly identify the feasible projects and could more easily pick and choose the right opportunities to add up to the desired value in the allotted amount of time until exit. We worked together to quickly evaluate a total of 130 different operational improvements, process improvements, and VA/VE opportunities across five sites. This included a workable improvements bridge to realise \$13 million-plus in savings over the next year with an estimated EBITDA impact of 300 to 500 basis points (See Figure 2).

2. MAKE HIGH-IMPACT/HIGHLY-CHALLENGING PROJECTS MORE DOABLE

Ideally, your impact/timeline matrix will reveal enough opportunity to generate the return you want in the time you have until exit. When this isn't the case, or when there are extremely high impact opportunities that fall outside of the timeline window or that require more effort or resources than you can feasibly invest, it's worthwhile to explore ways to expedite those opportunities and/or to reduce the difficulty level or implementation hurdles while still maintaining as much of the impact value as possible. This often starts by breaking down a project into more digestible chunks of work.

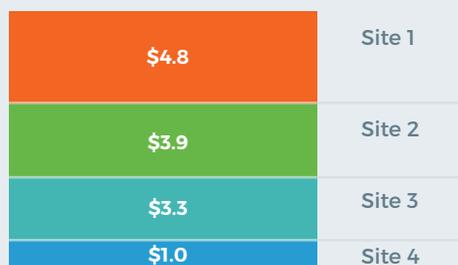
FIGURE 1

An Impact/Difficulty Matrix Visualises Value Creation Opportunities



FIGURE 2

A Workable Improvements Bridge Identified \$13M in Savings Over Four Sites



\$13M in savings

For One PortCo, VA/VE Projects Were a Source of Hidden Value

- 130 potential areas of savings
- 63 value add / value engineering projects totaling \$7.2 million
- 61 operational excellence improvements totaling \$5.8 million
- 6 business process improvement projects

Getting granular about the actual work that needs to be done can show you if portions of a project can be realistically accomplished. It also sheds light on the specific problems or issues that make a project difficult. When you better understand the problem, you can create a collaborative workplan for addressing it, which can help move a project from right to left.

In our PE client example, we found that developing sales processes standard work and systems was a high impact opportunity representing \$350,000 in combined savings and gross margin gains for the portfolio company. However, because of the skills required to implement these changes and to direct a large number of diverse employees in the new processes, the opportunity was slated as one of the most difficult on the table for the company to manage with its own resources. Even so, the PE firm found that it could unlock the opportunity and accelerate the gains by outsourcing the project, thus making the sales process work a viable and worthwhile pursuit that should soon return a direct impact on company value.

3. REDUCE COSTS OR FUNCTIONALLY IMPROVE PRODUCT MANUFACTURING PROCESSES

VA/VE—value add/value engineering—projects are improvements that go beyond traditional operational excellence or purchasing strategies to fundamentally change the way a product is designed or to alter the components and materials used. The end goal is to improve functionality or value for the end user while reducing the costs to get the goods out

the door. Considering that for a typical product, 50% to 70% of costs are attributed to materials, there is generally a lot of room for improvement in this area. And, when realised, those improvements have the potential to significantly impact gross margin, EBITDA, deal multiples, and overall profitability.

Still, these opportunities are often overlooked because decision makers tend to assume that they fall on the right side of the impact/difficulty matrix, demanding extensive time and resources to bring to fruition. While it is certainly true that some of these projects will require engineering rework, field testing, or regulatory approvals that will extend the timeline beyond what's feasible, others are far simpler in nature.

Some can even be considered quick wins. Indeed, in the PE firm example we've been discussing, almost half of the 130 projects we identified as doable within the holding period fell into the VA/VE category, and the quick wins included things such as reducing the screw count for attaching two components and removing the plastic bags from a component. Collectively, the VA/VE projects accounted for well more than half of the total savings opportunity for the firm.

This isn't always easy to do for people who are closest to the project. It's important to keep an open mind and be willing to consider new or different approaches.

The trick to finding these VA/VE projects is to step back, look below the water line, and think a bit differently about what types of design or material changes are actually possible within your allotted timeframe and with the resources you have that are easily accessible.

It's also wise to look for the low-hanging fruit. For example, conducting a parts count assessment is relatively easy to do and it can help you identify parts that can be consolidated or eliminated, which tend to be relatively simple design changes to make. Also be sure to look for processes that may be outside of an organisation's core competency areas and, as a result, may be inefficient to handle in house. Outsourcing these can free up internal capacity that can be put to work for much better returns.

A margin analysis is another worthwhile effort that can lead to significant VA/VE opportunities. With our PE client, we found margin improvement opportunities across several product families, including one product that the portco is currently losing money to produce. Within this particular product family, we helped the team identify 42 individual VA/VE projects with the potential to improve gross margin from -2% to 17% and generate nearly \$326,000 in annual savings. We helped the PE firm extend the potential savings even more by evaluating the potential for each VA/VE project to be implemented across the entire product portfolio.

4. ACCELERATE PROJECT EXECUTION

With the value creation potential well defined and the roadmap in place, the only thing left to do is to execute. Any “just-do-it” opportunities—those with the lowest difficulty level or quickest time horizons—should be assigned and implemented as quickly as possible. Even if the return seems nominal for each project, the cumulative effect can add up quickly, all for very little effort on the part of the team.

For those projects that require a more concerted effort, the keys to accelerating the execution process include:

- **Executing more projects in parallel.** At a single site, projects are often sequenced and spaced out over time. It is also typical for multi-site companies to embark on improvement plans at one site before moving on to the next. Right now, consider executing more aggressively and running several projects simultaneously to make up for any lost time during the pandemic.
- **Working at the point of impact.** Engage the experience and input of your front-lines operations people who are involved in running your business every day and who can ensure the maximum impact of each improvement.
- **Putting the framework of the solution in place quickly.** Avoid getting delayed by the minor nuances or details of the project. Remember that when time is of the essence, perfect can be the enemy of good.
- **Tracking progress and make it visible.** Keep everyone on the team informed, accountable, and on task.
- **Firing on all cylinders.** Whenever possible, leverage the synergies generated by combining engaged people, proven process rigor, and the right supporting technologies.

If there's ever been a clear case for speed, it's now

In so many instances, speed is key to any business win. And for private equity firms with exit dates looming, pulling out all the stops to expedite value creation right now is imperative. By quickly reassessing opportunities, being open to those that may require some outside expertise or fundamental (but viable) changes to product designs or materials, and using proven strategies to fast track implementation, you can get the return you want in the time you have. But don't wait. The time to get started is right now.

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