

## Client Profile

**Client:** *Manufacturer of artificial and natural sweeteners*

**Product Lines:** *Small construction equipment lines*

**Headquarters:** *United States*

**Revenue:** *>\$300 Million USD*

## Participating Client Functions

- Corporate Finance
- Manufacturing operations
- Supply Chain
- Contract Manufacturing Partners

## Expertise Used in Project

- Financial statement analysis
- Commodities Management
- Cost Modeling

*“We gained insight into our business in this project that we did not have before. If we had not done the project, we may have made the wrong decision for the company, because we were looking at only point estimates without considering the risk, as well.”*

VICE PRESIDENT OF FINANCE

A large food manufacturer considers the profit impact and risk of outsourcing all its manufacturing worldwide.



## Challenge

The president and the CFO of a food manufacturer of artificial and natural sweeteners had been given aggressive goals for increasing free cash flow (and company valuation) by their private equity owner. They needed revolutionary, not evolutionary change to meet their goals. They had several possible options, one of the boldest being to sell all three of their manufacturing plants to large contract manufacturers, so the client could buy, rather than make, its products.

A structural change of this magnitude would have tremendous financial and cultural effects on the client. How would each major metric on the financial statements be affected? How much financial benefit and increased valuation, would this option bring? How much risk would be associated with outsourcing these plants, versus the other strategic options the client's executive team was evaluating?

Hiller Associates and one of its consulting partners was retained to answer these questions and make a recommendation.

## Discovery and Solution

After researching and consideration the change, it became apparent that this was not a surgical move by the client, but a wholesale change that would effect every part of each of the client's financial statements.

HA created new, normalized financial statements (income statement, balance sheet, and cash flow statement). These new statements were first created to model the current state of the client (internally owned plants) and then expanded to include the new option (full outsourced contract manufacturing) the client was considering.

It was important that the HA models for financial statements could correctly replicate the client's current financial state. Working with the client's CFO, the new financial model was certified as accurate.

Meanwhile, HA's consulting partner, an expert in supply chain, was able to assess the supply chain impact of fully outsourced contract manufacturing. The partner was also able to collect the data inputs needed by Hiller Associates for the new state of the client (outsourced manufacturing).

Using the data from the consulting partner, HA was able to calculate both the one-time and annual effects on the client's financial statements, as shown below.

	Current State		Future State	Enterprise Benefit	
Revenue*	Current Product Revenue (\$280M)	➔	New Product Revenue (\$360M)	= \$23M	Profit on additional revenue
Product Cost*	COGS (\$170M)	➔	Reduced COGS – More Logistics (\$120M)	= \$50M	Cost of Goods Sold improvement
Sales, General, & Administrative*	Current Organization (\$30M)	➔	Sales / Marketing Organization (\$21M)	= \$9M	Leaner organization
One time effects*	Current Asset Value (\$250M)	➔	Assets Sold – Transition Cost (-\$275M)	= (\$15M)	Net Investment
			Current Valuation	+	Value Effect of \$82M annually and \$15M investment
				=	Increased Valuation

\* Numbers modified to protect client confidentiality

Moreover, HA's financial models were able to quantify the sensitivity of the client's future financial results to each major model input. Using these results, the client knew not only the reward associated with the outsourcing plan, but also the risk.

## Results and Impact

The HA financial model showed that the potential benefits of outsourcing all the manufacturing of the client would be significant, even on an annual basis. Furthermore, the expected value increase to the client's valuation was also significant. However, the risk associated with such a bold structural re-engineering of the company was also high. Knowing this information, the CFO and the President of the client were able to evaluate outsourcing versus other possible strategic options for meeting the client's investor's goals.

The client executives confidently decided to pursue another strategic option that provided somewhat less benefit, but was also substantially less risky than outsourcing.

### About Hiller Associates

Hiller Associates is a business performance consultancy that specializes in Product Cost Management (PCM), helping discrete manufacturing companies reduce product cost, whether the product is before or after launch.

Our practice sits in the nexus between design engineering, finance, purchasing, and manufacturing. HA has helped Fortune 1000 clients save tens of millions of dollars through our Product Cost Management engagements. If you have a challenge with Product Cost Management in culture, process, roles, or tools we would like to help.