



This bulletin is designed to provide our business partners and friends with valuable market and business insights.

The current edition of our bulletin contains two articles:

- 1) **Strategy-driven Spend Optimization vs. Category Sourcing**
- 2) **Trends in the private equity market – redirect commercial due diligence towards higher investor requirements**

In addition we provide you with selected news and highlights from our Lansdowne network.

1) **Strategy-driven Spend Optimization vs. Category Sourcing**

Recent global economic developments have opened up new opportunities to realize savings in sourcing of industrial goods & services, as prices are decreasing and exchange rate developments negatively affect the attractiveness of global sourcing. Strategy-driven spend optimization approaches help companies to leverage savings beyond traditional category sourcing initiatives, but their success is dependent on a set of critical factors.

Situation

Recent European and global economic developments have uncovered new potentials to generate savings in sourcing: A near to zero inflation rate of -0.2% in the Eurozone (Jan '15)¹ and falling production costs and prices for industrial products, partially driven by the plummeting of crude oil prices since June 2014 from over US \$100 per barrel to a low of US \$46 in January 2015², reveal opportunities to lower sourcing costs in the industrial sector.

An additional factor currently impacting the choice of the right supplier strategy is the €/€ exchange rate development: The weak EURO has lost around 19% in value compared to the US \$ in the last year³, making sourcing in global markets more expensive for European manufacturers. This development can affect the attractiveness of whole supplier markets and may shift price advantages from global suppliers to European suppliers.

Focusing on China as low-wage supplier market is therefore no longer sufficient. In recent years, the industrial sector in some Eastern European countries, such as Poland, Romania and Slovakia grew significantly. At the same time, quality and reliability of these suppliers are improving steadily, introducing sourcing alternatives to Western European industry.

Enterprises often do not leverage these potentials as procurement is many times based on long term contracts rather than periodic re-negotiations. Benefits and savings from falling industrial goods prices and new opportunities are therefore not realized.

Compared to traditional value creation initiatives, sourcing & spend optimization strategies generate rapid and impressive EBIT growth and cash flow



improvement with short payback periods of project costs (see illustration 1).

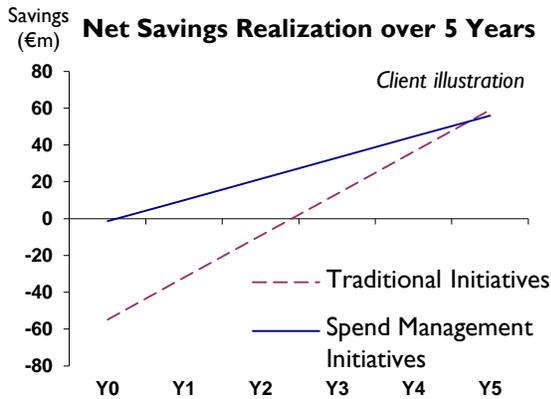


Illustration 1: Impact of Spend Optimization Initiatives

Consequently, sourcing optimization is an important and sensitive way (e.g. in comparison to headcount reductions) to lead companies to profitability and improved margins, especially for investment funds. Through the rise in secondary investments in the last years, companies have often already run through traditional operational efficiency programs; strategy-driven spend optimization programs can leverage savings where common restructuring and re-organization programs cannot realize further benefits. In consequence, sourcing optimization often is the single lever left to improve margins.

Spend & sourcing optimization initiatives, however, need to be executed with care, as unprofessionally managed cost reduction initiatives could negatively impact a company's strategy.

Key success factors in spend & sourcing optimization

The successful execution of strategy-driven sourcing optimization initiatives requires a set of key success factors:

- Understanding and incorporation of client's strategy into sourcing approach
- Complexity management

- Change management (buy-in of functions and client team)
- Total Cost of Ownership (TCO) approach
- Sustainability management

A first essential step for successful sourcing optimization is to fully understand the company's strategy. This is a prerequisite for defining the spend & supply strategy, identifying strategic suppliers and assuring that supplier changes will not have a negative impact on the strategy (see illustration 2).

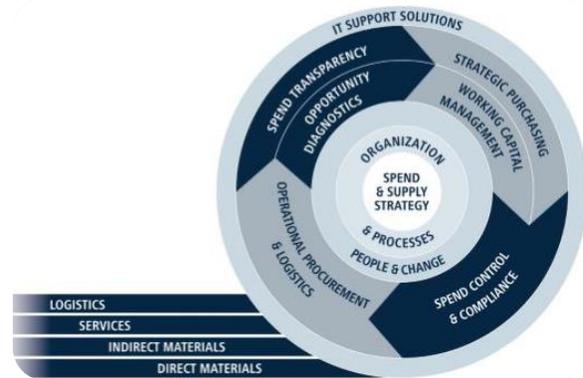


Illustration 2: Lansdowne's Procurement Wheel

In addition, a clear understanding of the strategy is the basis for the identification of the right levers. While category sourcing initiatives often only focus on commercial levers, strategy-driven spend optimization addresses a much broader portfolio of additional technical and process levers (see illustration 3).

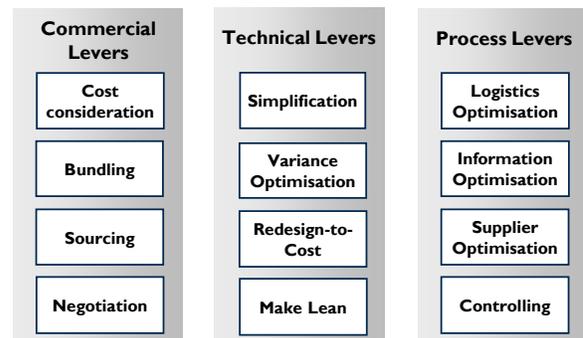


Illustration 3: Strategic Procurement Levers



In addition to a wider selection of levers, the understanding of the company’s strategy will enable the pursuit of a wider range of goals. For instance, not only will spend optimization cut costs, but it can also deliver additional benefits such as partnering with innovative suppliers and improving quality.

The application of technical and process levers significantly increases the complexity of sourcing optimization and requires the integration of various departments (e.g. Procurement, Research & Development, Production, Quality and Marketing & Sales) in the project team. In consequence, while category sourcing project teams often only bring in specific sourcing expertise, strategy-driven sourcing optimization requires experienced and heterogeneous project teams to manage far greater complexity and to meet the requirements of different departments and stakeholders.

Change Management is another crucial success factor in the implementation of strategy-driven spend optimization projects. Generating the required degree of transparency and level of data granularity for technical and process levers requires strong support from all departments since the applied levers operate at the core of the company’s business compared to the relatively simple commercial levers in category sourcing.

Another mistake often made in sourcing projects is the acceptance of inadequate financial modeling. Companies opt not to conduct a “Total Cost of Ownership” assessment in order to save time and achieve a quick win, without taking into consideration the long term effects. As a result, the implemented changes often do not represent the optimum solution.

Finally, many category sourcing programs finish without implementing proper sustainability management, thereby jeopardizing the achieved results. Effective sustainability management includes the definition of KPIs and the implementation of ongoing supplier performance measurement as well as internal compliance management to secure long term benefits.

Through its mastery of the strategy-driven spend optimization approach and the set of technical & process levers, Lansdowne is experienced at achieving sustainable, double digit savings percentages, which greatly exceed the savings potential of traditional category sourcing.

Lansdowne’s approach

Lansdowne has developed a holistic 6-module approach to address the challenges of complex strategy-driven spend optimization and to achieve savings & benefits far beyond the results of traditional category sourcing projects:

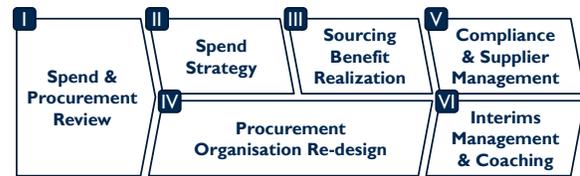


Illustration 4: Lansdowne’s 6-module spend optimization project approach

With a comprehensive toolkit for strategy-driven procurement and turnaround programs, Lansdowne supports its clients to realize rapid, significant & sustainable benefits & savings.

Conclusion

- Recent global economic developments have opened up new opportunities to realize savings in sourcing of industrial goods & services
- Strategy-driven spend optimization initiatives can leverage savings beyond traditional category sourcing approaches
- Their success is dependent on understanding the clients strategy, managing the high degree of complexity of additional technical & process levers and gaining buy-in of functions and the client’s team



- Lansdowne has developed a holistic 6-module approach to address the challenges of strategy-driven spend optimization and realizes high & sustainable savings for our clients

II) Trends in the private equity market – redirect commercial due diligence towards higher investor requirements

The German private equity market is currently experiencing a high transaction volume growth rate of 73%. The increasing number of players and liquidity in the market is stretching bidding to the limit. Commercial due diligences are hence facing much higher expectations from investors to support increasingly risky investment decisions. Thorough understanding of the target’s business model and a senior team with the right blend of subject matter expertise are key to success.

The German private equity market recently experienced high growth with 1,633 transactions in 2014, 22% more than the previous year⁴. The total transaction volume of 237bn EUR increased by 73%¹.

Illustration 5 shows the distribution of deals in the 1st half of 2014: The highest cumulated deal volumes have been taken place in the Communication Technologies sector (42.5%), followed by the chemical sector and consumer services and goods.

The boom is mainly driven by three factors:

- Very high liquidity at companies and private equity funds
- Excellent financing conditions from banks and debt funds due to very low interest rates
- Drive to achieve growth through acquisitions

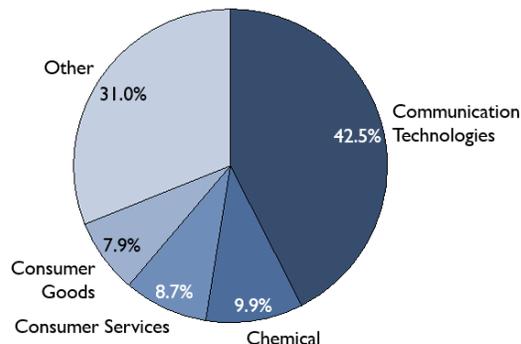


Illustration 5: M&A activities in Germany (1st half of 2014⁵)

These drivers have led to fierce competition for targets among investors (both private equity and strategic investors) due to higher availability of capital and lower return rate requirements to compete with alternative investment opportunities (e.g. loans, stocks, etc.). In consequence, transaction values have increased with two-digit multiples (EBITDA), while return rates and margins have shrunk.

Investment decisions in the private equity sector therefore are becoming increasingly challenging. A changed market environment with the increasing global nature of today’s business, transforming emerging market economics and higher exposure to financial and economic crises intensifies the risk exposure of investments. On the other hand, we observe more fierce competition for investment targets between investors. Commercial due diligences are hence facing much higher expectations from investors to support increasingly complex investment decisions.

Challenges & Key Success Factors

M&A activity brings substantial risks that need to be systematically identified and professionally managed. Statistics show that 60% of M&A deals destroy value for the acquirers⁶. This underlines the importance of a pre-acquisition due diligence. Downside risks have to be addressed upfront, such as overestimation of synergies and unrealistic growth rates. A thorough due diligence should also uncover potential upsides, such as cost savings, operational improvements,

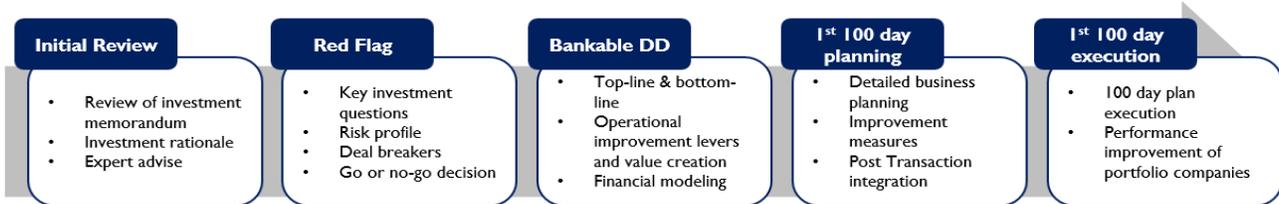


Illustration 6: Lansdowne Due Diligence Offering

turnaround & restructuring opportunities, capital optimization and profit maximization. Effective due diligence uncovers hidden levers and other drivers that may affect a deal's value.

Traditional commercial due diligence approaches often do not provide a solid and profound basis for negotiations and investment decisions since they lack value adding potentials and rigorous sensitivity analysis. The main reasons for these deficiencies are:

- Focus on top-line and market dynamics research, barely scratching the surface to conduct deeper, value added analysis
- “Due diligence factory” with junior consultants and copy & paste approach
- Overreliance on desktop research and secondary sources

We believe that understanding the client's business and overall strategy is key to conducting a successful due diligence.

Consequently, Lansdowne follows a tailored commercial due diligence approach that significantly differs from traditional practice. The main characteristics are:

- Thorough understanding of business model and mechanics related to competition and market dynamics
- Integrated view that considers both top and bottom line
- Identification of operational improvement levers and value creation

- In-depth risk analysis and stress testing
- Financial modeling with sensitivity analysis in close cooperation with financial due diligence

We believe that another key success factor in providing due diligence services lies in an appropriate team and resource set up. Every due diligence highly depends on the team and its ability to understand the business' long-term strategy, growth plan and technical insights. Therefore teams should consist of senior consultants who provide a business and strategic understanding as well as at least one subject matter expert with in-depth understanding of the industry. Our experience shows that these industry experts are key to successfully conducting a due diligence and more than one expert per team is recommended to use their industry insights and technical expertise in the most efficient way possible.

Lansdowne's resourcing and leadership model combines senior partner expertise with industry insights through subject matter experts and follows our entrepreneurial driven philosophy:

- Tailored engagements led by Partners who are actively involved in all phases from interviews to report development
- Approach based on sound business acumen
- Experienced, multinational consultants
- Senior industry experts and thought leaders



- Delivery of real insights by leveraging wide network of subject matter experts, industry specialists and executives
- Global coverage

Lansdowne successfully blends senior expertise with industry know-how to provide a tailored team for the delivery of high-quality work.

Lansdowne’s Due Diligence Offering

Our business model is based on sustainable client relations and high responsiveness to clients’ day to day needs throughout the entire transaction process. Hence we provide commercial due diligence services covering the whole investment side, including initial review of info memorandum, red flag due diligence, full commercial due diligence with bankable report, 100 day planning and execution as well as performance improvement of portfolio companies (see illustration 2).

Lansdowne’s Munich office has conducted over 50 due diligence reports across multiple industry segments over the past three years (see illustration 3).

A selection of industries in which Lansdowne has conducted due diligences over the past years illustrates our broad expertise:

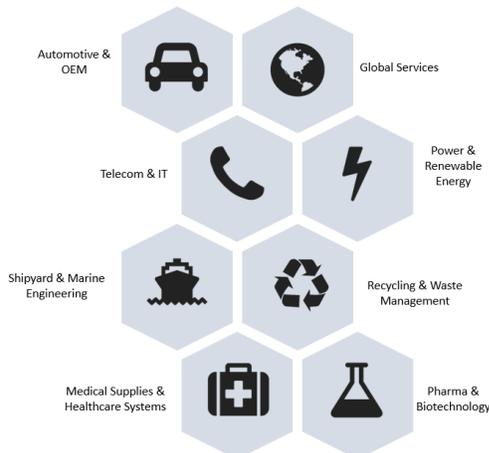


Illustration 7: Lansdowne’s Track Record

Automotive, Biotechnology, Construction, Electro technology, EMS, Defense, Healthcare, Hotel, IT, Luxury Goods, Machines, Marine Engineering, Medical Supplies, OEM, Pharma, Plastics, Power, Printing Services, Recycling, Renewable Energies, Shipyard, Telecom, Utilities and others. Lansdowne Munich has led these projects across the globe in Asia, Central & Southern Europe and the MENA region.

Conclusion

- The increasing number of players and liquidity in the German private equity market is stretching bidding to the limit
- Commercial due diligences are hence facing much higher expectations from investors to support increasingly risky investment decisions
- Traditional commercial due diligence approaches often lack value adding potentials and rigorous sensitivity analysis and do not meet today's investor requirements
- Lansdowne follows a tailored commercial due diligence approach that blends senior expertise with industry know-how to deliver high-quality & value adding services to investors
- Our thorough due diligence approach not only addresses downside risks, but also generates additional value by uncovering potential upsides, such as cost savings and turnaround & restructuring opportunities



Recent News



Lansdowne conducted the commercial due diligence of VUD for VERTIKOM and advised VERTIKOM on the successful acquisition of VUD Simply Channel. Founded in 1992, VUD focuses on merchandising services (i.e. rack-jobbing). Success factors of VUD are close relations and cooperation with electronics specialists. VUD GmbH manages marketing, sales and distribution activities for manufacturing companies. These services are offered exclusively as well as in team packages, which allows to optimize efficiency and pricing through bundling synergies.



SEAFORT ADVISORS

Lansdowne carried out the commercial due diligence of Emdor Werft- und Dockbetriebe (EWD) for Seafort Advisors and advised Seafort on the successful acquisition of EWD. The company, now Emdor Werft- und Dock-GmbH, focuses on maintaining and servicing of naval, trade and coastguard vessels as well as activities in the offshore sector. The company is considering to enter a new market by offering megayacht maintenance and renovation services.



Lansdowne also conducted the technical, financial and commercial due diligence of an American biotechnology company for a Saudi Arabian investor group and advised them on the successful acquisition of the target.

Lansdowne recently won a bid against major international consultancy firms for a large business planning and industry build-up project in the telecom and infrastructure sector in the Middle East.

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