Creating Value in Specialty Distribution

TandLA

Transportation and Logistics Advisors, LLC

Agenda

- **Why Supply Chains Are Important for Distribution Companies**
- *TandLA* Supply Chain Improvement Approach
- Examples of How PE's Can Harvest Value

Distributors are marketing & sales companies, enabled by a supply chain and supported by a back office

Marketing & Sales	Supply Chain
• Create value servicing customer and manufacturer needs – Support customers with products, value added information and other services – Provide channel to market and value added feedback to manufacturers • Manage a sales channel	• Procurement and sourcing • Transportation – Inbound – Outbound • Warehouse operations • Inventory management
Back office functions – accounting, legal & compliance, human resources, and general management	

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Large distributor supply chains are often highly engineered, but mid-market distributors tend to be less sophisticated

Large Distributors	Mid-Market Distributors
• Supply chains planned and optimized for lowest total delivered cost – DC's size and location designed by optimization tools – Inventories planned using optimization tools – Transportation optimization ➢ Private fleet utilization optimization ➢ Intelligent 3rd party carrier sourcing • Supply Chain execution automated by sophisticated tools – Warehouse Management Software – Transportation Management Software – Order Management Software – Inventory Management Software • Continuous improvement supported by Business Intelligence (BI) databases and analytical capabilities • Rich set of KPI's and metrics for managing the supply chain decisions and performance • Emerging focus on using supply chain as a competitive weapon – Do what competitors can't – Offer multiple delivery/price options that differ by SKU	• Built with a Marketing focus – Focus on adding value in a specialty market – Organizational strength in capturing and servicing customers • Distribution centers based on history – Not based on total delivered cost – Often located close to where founder lived and company began • Few sophisticated planning and execution tools – Optimization tools – Automated execution tools – BI databases and analytical tools • Limited service/cost options • Limited/no use of the supply chain as a competitive weapon

Many mid-market distributors also tend to be not well positioned for the future…

Supply Chain Shifts	Geography Shifts	Competitive Shifts
• eCommerce Growth – Demand for smaller, more expensive outbound shipments – Increasing need for fulfillment centers closer to customers – Increasing need for multiple outbound service levels • Warehousing Costs – Cost of small facilities near metro areas rapidly increasing – Growth in warehouse automation • Transportation Costs – Not changing equally by mode or lane – Significant accessorial fee increases • Transportation Options – New third-party services available	• Sourcing – Shifting import origin (out of China, into other SEA and Mexico) – Shifting domestic sourcing (growing, moving south) • Market/Population – Shifting out of northern states (e.g., New York, Illinois) and into sun belt states – Shifting metro areas, out of large old cities (e.g., Chicago and New York) and into high growth cities (e.g., Austin and Nashville)	• Existing Competitors – Adding new products and services – Offering multiple service levels – Selling “virtual” inventory/ SKUs • New Competitors – Amazon.com and other eCommerce – Others starting with a clean slate or new business model

… But, the barriers to a mid-market distributors supply chain competing equally with larger competitors are coming down

Previous Reasons for Lack of Supply Chain Sophistication	Barriers Coming Down
• Focus has been on Marketing, Selling and Customer Service • Focused on daily execution – supply chain viewed as something to do after the sale • Cost prohibitive supply chain sophistication technology and tools • Cost prohibitive to add high power supply chain management • Costly to change a warehouse network • Lack of knowledge of options for transporting, storing and delivering products – as well as options for creating value in the supply chain • Lack of analytical capability	• Cost of technology/software is declining, more accessible to mid-market companies – Low cost tools available (e.g. BI tools) – Software as a service – API integration – 3rd party options available • New capabilities available – Technologies created for eCommerce supply chains – New transport capabilities created for eCommerce supply chains and can be used for non-eCommerce – Drop ship from manufacturer using Heavy Goods Delivery Services, or alternative parcel services – Zone skip parcel or LTL – Express delivery services – Same day services – Crowd sourcing services • Management skills and analytics available from third parties

And improving mid-market supply chains can add value to both customers, and to owners

1. **Improved Cash Flow –** near-term cash from execution-based changes, project payback may be one to three months, tactical changes can continue to grow cash flow for years
   - Reduced transport costs, inbound and outbound
     - New pricing
     - Better use of lowest cost providers
     - Better use of private assets
     - Shift to lower cost services
     - Improved productivity
   - Lower warehouse and operation costs
     - Better use of labor
     - Better use/lower cost warehouse equipment
     - Better use of facilities
   - Lower inventory levels
     - Liquidate low turn SKUs
     - Reduce procurement to increase turns of moderate turning SKU
     - Sell virtual inventory
2. **Higher EBITDA**, both now and forecast
   - Changes rolled out over time
   - Plan placed in the data room to support EBITDA projections at time of sale
3. **New Service and Product Options,** adding value, better serving customers

Benefits from an improved supply chain come from three sets of changes, over three different time frames

Initiative Type	Implementation Time Frame	Cost of Change	Description
Execution	• A few weeks or months	• No required CapEx • No required OpEx	• Changes to internal processes, measures and metrics • Changes in transportation procurement • Changes in asset productivity • Changes in inventory levels
Tactical	• Three to six months	• No required CapEx • OpEx likely required	• May require IT/programing changes • Changes to support new business processes • May require severance or lease cancelation fees to increase productivity • May require new purchase order quantities • May require new price/volume structure for customers
Strategic	• More than a year	• CapEx and OpEx likely required	• Significant changes in the supply chain • Potential for CapEx for facilities or equipment • Potential for OpEx to move inventory and people

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TandLA has a two Phased approach to improving mid-market specialty distributor supply chains

TandLA Supply Chain Improvement Approach

Phase 1: Identify Opportunities

- Traditional "As Is-To Be" assessment
- Sizes the opportunity for change
- Identifies the changes/initiatives required to capture the opportunity
- Categorizes and ranks the change initiatives
- Simultaneously assesses Execution, Tactical, and Strategic change opportunities

Phase 2: Implementation Planning

- Prioritizes and sequences change opportunities
- Creates specific action plans for each change initiative, including:
  - Management responsibility for each initiative
  - Timelines for initiative – begin, end, and benefits
  - Investments and resources
  - Detailed action plans
- Creates a program management plan to:
  - Keep initiatives on track
  - Monitor costs/benefits

Phase I focuses on not only the opportunity gap, but also what initiatives are required to yield the benefits

Potential Phase I Supply Chain Change Initiatives

Execution	Tactical	Strategic
• Bid freight • Switch to a 3PL with more scale, options and technology • Reign in rogue spend • Minimize premium freight (e.g. switch Express to Ground) • Minimize low turn/low margin SKUs • Change shipping and receiving day of the week	• Use BI database to identify business changes • Change price/volume structure to customers to fill out freight and sell more product • Change order to delivery cycles • Change procurement order quantities to fill out freight • Utilize drop ship options • Utilize domestic consolidation • Utilize overseas consolidation • Change private fleet to dedicated • Change private fleet into a for-profit carrier • Change ports and flows into DCs • Change warehouse labor sourcing • Reign in accessorial charges with changed behavior, shipping • Shift low turn SKU's to direct with premium freight	• Change warehouse/fulfillment network • Add third party facilities in smaller markets • Shift third party facilities to in-house in high volume markets • Add multiple service/delivery options • Add low volume SKUs to portfolio with drop ship model • Add order management tools that recommend added product to an order and discount based on freight • Add automation in high volume facilities

Phase II Example Implementation Plan – Dedicated Trucking RFQ Process

Week	1	2	3	4	5	6	7	8	9	10	Completion Date	Responsibility
Project Kickoff Meeting											4/16	
Develop Initial Bid Package, Shipment Database											4/26	Jeff R.
Identify Companies To Invite To Bid											4/26	Jeff R.
Deliver RFQ Package to Potential Providers											5/3	Ellen Y.
Determine Options For Private Fleet Trucks, Drivers											5/10	Jeff R.
Review Submitted RFQs											5/24	Jeff R.
Negotiate With 2-3 Top Bidders											6/7	Jeff R.
Develop Conversion Plan											6/7	Ellen Y.
Finalize Contract Terms and Conditions											6/14	Jeff R.
Transition to Dedicated Provider											6/21	Ellen Y.
Ongoing Measures and Metrics											6/21	Kevin W.

▲ Change Committee Meetings

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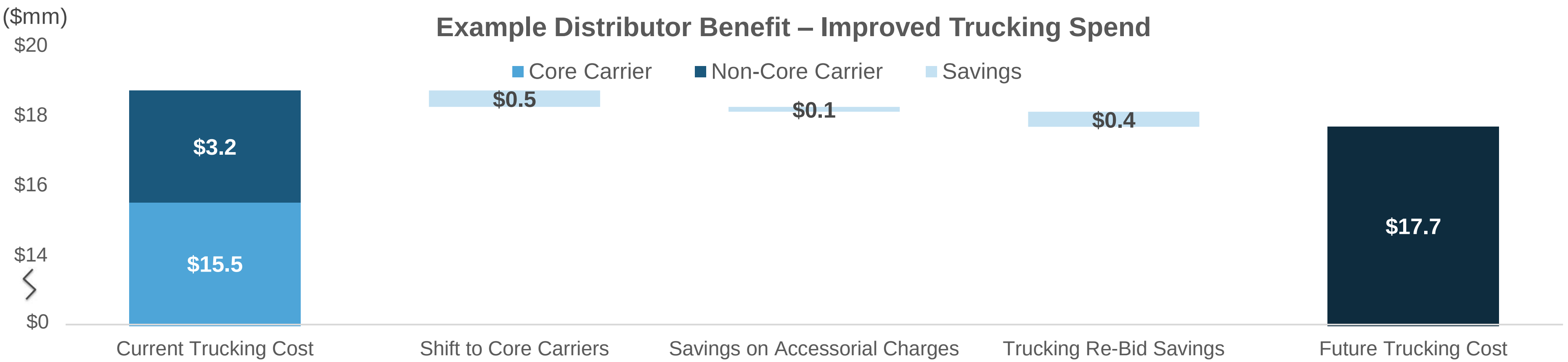
Execution Changes
Cost savings from re-bidding purchased transportation and better managing load tendering, improved EBITDA by 3.1%

Example Company: Lower mid-market PE owned distributor

Company Background	Tactical Improvement Selected	Results
• Lower mid-market PE-owned distributor • Revenue: $259.2mm • EBITDA: $33.8mm • Transportation spend: $18.7mm	• Reduce rogue transportation spend • Rebid transportation • Include accessorial fees in carrier selection process	• Monthly transportation savings of $87,000 (5.6%) • EBITDA increase of 3.1% • At 8.5x EBITDA, savings was worth $8.9mm to valuation • No CapEx or OpEx required



Current Trucking Cost
- Current trucking spend of $18.7mm
  - $15.5 based on routing guide
  - $3.2mm “rogue” non-core carrier spend

Shift to Core Carriers
- Non-core carriers ~14.6% more expensive than core carriers
- Adherence to load tendering process saves excess non-core carrier spend of ~$465,000, or 2.5% of current trucking cost

Savings on Accessorial Charges
- Improved accessorial charge management and consideration in bidding saves 8.9% of accessorial charges
- Savings of ~$145,000, or 0.8% of current trucking cost

Trucking Re-Bid Savings
- Testing the market through a competitive bidding process
- Savings of ~$430,000, or ~2.3% of current trucking cost

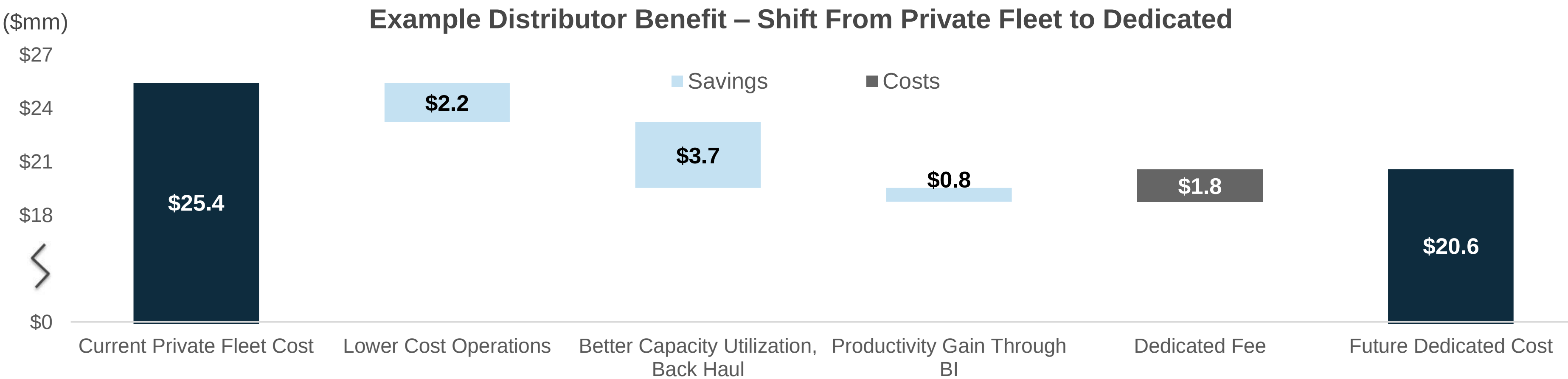
Future Trucking Cost
- Future spend of ~$17.7mm
- Savings of ~$1mm or about ~5.6% of current trucking cost

Tactical Changes
Switching to a dedicated fleet improved EBITDA by 9.5%

Example Company: Mid-market PE owned specialty distributor

Company Background	Tactical Improvement Selected	Results
• Mid-market PE-owned specialty distributor • Revenue: $450mm • EBITDA: $51mm • Transportation spend: $31.4mm • Private fleet percent of transp. 81% • On-time rate: 92.7%	• Improve efficiency and productivity of private fleet. Options include: – Outsource to a dedicated provider – Add systems, processes, and management to make private fleet world class • Option selected: convert to a dedicated trucking provider	• Total transportation savings of $4.9 mm (19.1%) • Contracted minimum on-time rate: 95.5% • EBITDA increase of $4.9mm (9.5%) • At 8.5x EBITDA multiple, increase of $41mm to valuation

Example Distributor Benefit – Shift From Private Fleet to Dedicated



Current Private Fleet Cost
- Private fleet of 51 trucks, company drivers
- Spend of ~$25.4mm

Lower Cost Operations
- Scale, processes to lower truck acquisition, maintenance & fuel costs
- Lower driver recruiting and compensation
- ~8.6% savings

Better Capacity Utilization, Back Haul
- Dedicated needs 45.7 avg. trucks
- Use 43 trucks 80%, flex to 51
- 8 avg. trucks brokered out when not needed
- ~14.6% savings

Productivity Gain Through BI
- Improved fleet productivity
- Improved on-time performance
- ~3.1% savings

Dedicated Fee
- Dedicated provider management fee
- ~9.8% of expected transportation spend
- ~7% of historic spend

Future Dedicated Cost
- Dedicated future spend of ~$20.6mm
- Savings of ~$4.8mm, or about ~18.9%

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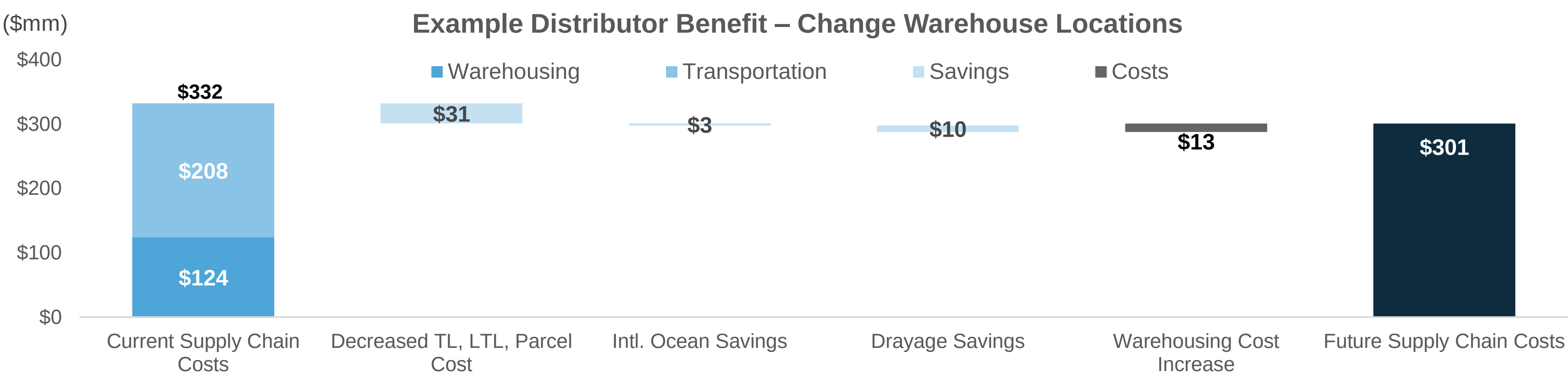
Strategic Changes
Close a St. Louis distribution center and replace with one in southern California, transportation savings dwarf facility costs

Example Company: Large PE owned distributor

Company Background	Tactical Improvement Selected	Results
• Upper mid-market PE-owned distributor • Revenue: $1.86bn • EBITDA: $176mm • Transportation spend: $208mm • Warehousing spend: $124mm • Total Tran & WH spend:$332mm	• Warehouses in Atlanta and St. Louis served through port of Savannah • Switch from St. Louis to Inland Empire to lower transportation costs, despite higher warehousing costs • Base case moving costs of ~$63mm • Reduced moving costs of ~$24mm	• Change-over costs of ~$24mm recovered in 9.3 months • Improved order to del. & on-time rates • Supply chain savings of ~$31mm (9.4%) • EBITDA increase of 18% • At 8.5x multiple, increase valuation $266mm



Current Supply Chain Costs
- Current supply chain spend of ~$332mm
  - $208mm transportation spend
  - $124mm warehousing spend

Decreased TL, LTL, Parcel Cost
- Savings of ~26% from shorter length of haul to West Coast
- Increase of ~6.5% to Upper Midwest
- Combined savings of $31.1mm

Intl. Ocean Savings
- Lower container shipping costs through Port of LA/LB vs. Savannah

Drayage Savings
- Lower drayage cost through Port of LA/LB

Warehousing Cost Increase
- Inland Empire more expensive than St. Louis
  - Rent 67% higher
  - Labor 24.8% higher
- Additional $13mm of warehousing costs

Future Supply Chain Costs
- Future spend of ~$301mm
- Savings of ~$31mm or about ~9.4% of current cost

Strategic Changes (example continued)
Change made viable through non-traditional options that lower change-over costs, and shorten pay back time

	Traditional Change ($M)	Trade Labor with WH 3PL	Trade Lease and Labor	Integrated 3PL[1]
Description	Close STL WH, layoff all workers, lease new CA WH	Have a WH labor 3PL take workers in exchange for providing labor in new CA facility. Pay rest of lease.	Have a WH labor 3PL take workers in exchange for providing labor in new CA facility. Pay real estate company to take STL lease, in exchange for CA WH lease	Rent space in 3PL WH, pay only for space/labor used. Shift inventory slowly to CA over remainder of STL lease, shrink STL workforce by attrition
Startup Costs (Recruitment/Management)	7.4	None (Labor Provided)	None (Labor Provided)	None (Labor Provided)
Severance Pay (19.6% annual labor costs)	3.6	None (Labor Offloaded)	None (Labor Offloaded)	25% of full severance pay, workforce dwindles by attrition until WH closes
Double Lease Payments (3 years on lease left)	37.5	Remaining STL lease paid	None (Lease Taken)	Pay double labor/rent, but these are offset by paying less on rent/labor in CA due to slowly scaling up
Inventory Moving Costs	14.2	Must pay to move inventory to CA	Must pay to move inventory to CA	Must pay to move some inventory to CA, but rest worked off over time
Brokerage Fee (26.8% of remaining STL lease)	-	None	Full	None
Total Cost	**$62.7 M**	**$51.7 M**	**$24.2 M**	**$37.1 M**

Note: (1) Full transportation benefits don't appear until end of STL lease

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