Divestitures and the Threat to Supply Chain Performance

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INNOVATION THROUGH PEOPLE, PROCESS AND TECHNOLOGY

When companies increase focus and resources on core capabilities to improve their service offerings and increase shareholder value, divestitures can often occur as a result. A major transition that impacts all areas of a business, including supply chain reliability and efficiency – divestitures have the potential to be positive or negative. With increased regulations, unstable market conditions and capacity concerns affecting today's shippers, it is near impossible for a newly divested company to achieve all of its goals without the expertise and support of a third-party logistics (3PL) provider experienced in that area.

State of the Industry: Divesting Today to Drive Strategic Growth Tomorrow

Today's corporate divestitures are often motivated by a desire to unload non-core, low-growth assets. According to a recent survey[1], the two leading strategies driving this market today are divesting segments deemed to be capital intensive, or those which are not aligned with a company's core business. These motivations suggest an attitude change towards divestures – one that primarily views the tactic as a necessity for growing core business units. As such, divestitures are reportedly increasing – a trend that is likely being fuelled by a narrowing strategic focus on core assets and reactions to volatile marketplace changes. Among companies that divested non-core assets over the last 24 months, the reasons for pursuing a carve-out included:

» Limited growth potential, cited by 37% of the surveyed executives;

» Non-synergistic products, mentioned by 30% of respondents;

» Poor operating performance, listed by 22%; and

» Weak market position, chosen by 11%.[1]

> "As corporations realize that a strategic logistics partner can better operate as an extension of their existing infrastructure, as opposed to relying on a transactional provider, 3PLs are experiencing a heightened demand for strategic outsourced solutions during the uptick of M&A activity."
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> – MIKE CHALLMAN, VICE PRESIDENT OF NORTH AMERICA OPERATIONS CLX LOGISTICS, LLC

Another 2015 report[2] indicated that expectations remain "sky-high for increased divestments of private equity portfolio companies, with about three quarters of private equity firm respondents, up from two-thirds last year, anticipating an accelerated level of exits within the next 12 months." On the corporate side, the report saw an increase in the number of company respondents expecting to shed business. This increase means a higher demand for third-party logistics providers with experience supporting newly divested companies, as their ability to maintain corporate continuity and supply chain performance during transitions is vital to the divested company's livelihood. This reliance is also turning 3PL providers into long-term and enterprise-wide partners.

Key Supply Chain Performance Challenges Caused by Divestitures

While restructuring assets of a business portfolio can help sharpen strategic focus for companies, divestitures also create challenges for supply chain executives who are tasked with ensuring the performance of new, smaller companies. Among these challenges is the potential for supply chains to become disrupted in several ways:

» Expertise provided by the selling company will no longer be there for the new, smaller divestiture;

» Staff size will decrease and employees may not possess skills in all areas, causing capability gaps; and

» Remaining staff will have to wear more hats to make the divested business run smoothly.

These major operational challenges, when not mitigated by an outside expert or combatted by the additional resources gleaned from a 3PL, have the ability to hinder the four major goals set forth for the typical divestiture, namely: maximizing price, minimizing disruptions to the retained business, keeping capabilities away from competitors and handing the buyer something that can be operated successfully from day one. In fact, dependent upon which report is consulted, Merger and Acquisition (M&A) initiatives, which include divestitures, have a failure rate of anywhere between 50 and 85%[5]. This statistic, while staggering, highlights the acute need for an experienced party to be involved.

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The Critical Role of a 3PL in Capturing Full Divestiture Value

A 3PL provider is a firm that offers customers with outsourced, or "third party", logistics services for part or all of their supply chain management functions. Logistics can include elements of warehousing, transportation management, reporting and analytics, forecasting, freight rate negotiation and much more. In support of a corporate divestiture, an experienced 3PL provider can offer a myriad of benefits, including:

» Immediate expertise and support in areas where a divested company has lost talent and insight;

» Valuable carrier relationships and advanced knowledge for optimizing supply chain performance;

» Input on best practices that have been gleaned from similar transitions with other shippers;

» Assistance with rapidly evolving shipping requirements, domestic and international; and

» The potential opportunity to convert a significant portion of operating costs from fixed to variable.

While each of the aforementioned benefits is a critical component of the value that a 3PL provides, the most important element is a 3PL's keen awareness of the service requirements needed across the supply chain. This industry intelligence helps ensure that the divested company has accounted for all workforce needs before, during and after the transition. This intelligence, combined with the ability to quickly and effectively fill gaps, is what maintains a seamless and high-performing operation – making 3PL assistance critical for capturing maximum divesture value, from day one.

1

Conduct a Frank Assessment

2

Effectively Leverage a TSA

3

Develop a New Supply Chain Model

4

Implement, Review and Adjust as Appropriate

A 3PLs Guide to a Successful Divestiture Rollout

STEP 1

Conduct a frank assessment of needs, requirements and capabilities in your 'new world'

The quicker a divested company recognizes that what worked previously may not work anymore, the faster and smoother the transition will be. This begets the need to set the overall strategy for the divestment by way of an exercise, called "capability scoping." This assessment identifies the most important capabilities for which the newly divested company needs to account, which may include functions such as Procurement, Purchasing, Accounting and even Supply Chain Operations itself. Some key questions to consider during this step of the divesture include[3]:

» What essential systems and processes will remain in place under the TSA, and for how long?

» Will existing arrangements with customers and suppliers still be valid?

» What impact will the divestiture have on both established manual and automated systems?

» How can you continue to motivate and inspire staff during the stress of a divesture?

» In which of these critical areas can the help of a 3PL be leveraged?

A proactive approach allows divested companies to uncover and fill capability holes before it's too late, by tapping into the capabilities of its 3PL provider. The company will not only benefit from its providers' expertise, but also from the ongoing upgrades and best-in-class improvements in which the leading 3PLs regularly invest. This approach also helps define career trajectory for the company's existing workforce and jumpstart the critical process of either retaining existing people and processes or redefining functions. A reported 93% of surveyed executives noted that maintaining the morale of employees of the business unit being carved out, was a significant issue[1].

Consider the top four areas of concern for the divested company in its 'new world' and the key functions that must be maintained, either by the new company or with the support of a 3PL.

Capability Assessment for the 'New World'

AREA OF CONCERN	KEY FUNCTIONS
Operations	» Operational planning and staffing » Facility readiness » Material handling and transportation
Technology	» IT infrastructure » Transportation Management Systems (TMS) » Warehouse Management Systems (WMS) » Finance & Accounting Systems
People	» Job transitions for existing or outsourced employees » Communications to customers about situation » Engagement with vendors to commence a new relationship
Project Management	» Workflow coordination » Budget, performance and measurement » Scope and timeline coordination » Transfer of processes

When utilized properly, a Transitional Service Agreement (TSA) can offer important benefits to a newly divested company, including a faster close, smoother transition, managed costs and a cleaner separation.

STEP 2

Leverage the support of a Transitional Service Agreement judiciously and wisely

When utilized properly, a Transitional Service Agreement (TSA) can offer important benefits to a newly divested company, including a faster close, smoother transition, managed costs and a cleaner separation. Overreliance on a TSA however, is a mistake companies sometimes make. Made between a buyer and seller, a TSA sees that the 'mother-ship' provides support to the divested company over a defined time period after the separation. This support may include central services like accounting, IT, procurement and human resources, but can cover just about any activity. When companies rely too heavily on this support, they may miss the window of opportunity to quickly and effectively establish the services and activities they will need to deliver on their own after the TSA ends.

A recent report[1] outlines typical organization practices for providing TSAs, emphasizing the importance for divested companies to plan wisely if they will be using a TSA and to be ready to operate without one, sooner than later.

» 39% like to avoid TSAs if possible;
» 25% like TSAs to facilitate divestures or manage costs;
» 22% indicate it's a common practice in order to sign up the buyer; and
» 14% never provide TSAs.

Just as crucial as starting off on the right foot is to establish a process early-on for assessing progress, measuring results and making necessary adjustments.

STEP 3

Develop a customer-centric supply chain model

Upon assessing your needs and properly leveraging the TSA, a 3PL can help the divested company develop and implement a new and detailed supply chain model. This effort not only accounts for the company's new set of demand signals, with different volumes and order patterns, but establishes a realistic implementation timeline for the transition from 'mothership' support to independent status.

Here are some of the key questions to ask when assessing your supply chain:

» How have your supplier and customer networks changed with the divestiture?

» Have you lost any network synergies as a result of separating your supplier base from that of the 'mothership', and if so, in what areas?

» What is the status of your contracts, rates and relationships with logistics service providers?

» What have you communicated to your key customers with respect to what you think they should expect from your 'new' supply chain?

» What specific expectations or concerns do your customers have about it?

» What is the growth trajectory for the divested company in the next 1-2 years? 3-5 years? 5+ years?

» What will business look like that the supply chain must grow and evolve to support?

» What key performance metrics do you have in place for tracking supply chain performance, to ensure it meets the needs of both internal and external stakeholders?

STEP 4

Integrate new model, review progress, and continuously improve performance

Just as crucial as starting off on the right foot is to establish a process early-on for assessing progress, measuring results and making necessary adjustments. Even the best laid plan that rigorously follows the first three steps outlined here is not going to remain unscathed by the vagaries of real life. So it is important to have several mechanisms in place to track performance.

One of those areas is Key Performance Metrics. The only way to know for certain that operations are going well or going south, is to measure, measure, measure. Effective metrics are specific, unambiguous and directly related to business goals.

Another important aspect for checking progress is to conduct regular, deliberate reviews. Representatives for critical processes and functions, whether they are internal resources or an outside party such as a 3PL, must meet regularly to review integration progress. It can be tempting to think, there is no time for that; too much work to do – but that would be a mistake. Taking sufficient time to review what's working and what isn't working is the only way to ensure your direction continues to be the best course.

Lastly, setting challenging but achievable goals is essential to keeping everyone aligned with the correct priorities. It almost goes without saying that a divestiture brings with it a raft of expectations. In order to turn those aspirations into results, a set of goals that addresses both near- and long-term is needed. Those goals should be subject to assessment through both metrics and regular review.

Based upon metrics tracking and regular reviews of progress toward goals, it is important that the divested company be ready and able to make adjustments to its plan. One or more of the assumptions made earlier in the process may prove to be inaccurate or may become outdated. For example, a fair assumption may be that relationships and rates with carriers may remain 'as is', only to find that some of the incumbents have taken the opportunity to use the divestiture activity as a reason to seek a rate increase.

Consider the key benefits a 3PL can add to a new supply chain model, ensuring success along the way.

> "As the M&A market experiences significant stimulation after nearly a decade, it's important to credit divestitures, when managed correctly, for serving as a vital asset optimization strategy. This tactic of 'letting go', is how many companies are growing, even thriving; it offers an opportunity for revival. Ensuring its success is what 3PLs do best."
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Ensure Reliability and Efficiency with 3PL Support

BENEFIT	PATHWAYS TO SUCCESS
Optimize Performance with Market Intelligence	» Use the 3PLs knowledgebase to assess carrier rates against the market, in order to determine if the divestiture creates risk of increased costs » Determine where specific functions should best reside in the new organization. Centralized? Decentralized? Performed by 3PL? What is best practice? What are your competitors doing?
Bolster Organization with Top Talent	» Leverage the knowledge and experience of logistics management professionals » Gain access to a large group of engineers, analysts and IT specialists » Utilize well-qualified supply chain operators to handle your day-to-day tasks
Transition Costs from Fixed to Variable	» Lead a cross-functional initiative to tackle cross-cutting opportunities such as shared-service and outsourcing operations[4] » Identify elements of the supply chain that can be performed effectively by the 3PL and which can be tied to volumetric measures as transaction costs » Consider developing a shared savings model with the 3PL as incentive to bring forward creative cost improvement ideas

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Mike Challman leads ChemLogix' Managed Services throughout North America, including freight management operations, benchmarks, bids and carrier procurement, rail fleet operations and brokerage services. Prior to CLX Logistics, Mr. Challman spent more than 20 years in the transportation industry, most recently serving as Senior Director, Transportation Management at DHL/Exel Supply Chain. His multifaceted logistics background includes leadership positions with Burnham Service Corporation, ROCOR Transportation and Schneider National Carriers, in addition to experience in customer service, solution development, project management and continuous improvement programs.

ABOUT CLX LOGISTICS

CLX Logistics LLC is a global provider of comprehensive logistics management, technology, and supply chain consulting services to a broad base of industry verticals. The global company, with offices in North America and Europe, is dedicated to solving its customers' most vital logistics challenges by leveraging a broad range of industry expertise, best-of-breed technology and a personalized, high-touch approach to deliver measurable, sustainable value.

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Conclusion

The strategic nature of any divestiture, merger or acquisition means there is time to prepare, and as such, supply chain leaders can ensure a seamless and high-performing supply chain before, during and after a divesture occurs by proactively embracing the four keys to a successful transition:

» Conduct a comprehensive situation assessment versus new requirements;

» Utilize transitional service agreements wisely and have an exit strategy;

» Detail and implement the new supply chain model;

» Review and continuously improve performance; and

» Leverage the guidance, expertise and support of a 3PL provider.

These steps not only set up both the mothership and spinoff for a successful transition, but allow both organizations to achieve their divestiture goal: to focus more strategically on high-growth portfolio assets.

1 Divestitures Survey Report, Deloitte, 2013

2 M&A Trends Report, Deloitte, 2015

3 Ensuring B2B and Supply Chain Continuity at Divestiture, GSX, 2013

4 Profitably Parting Ways: Getting More Value from Divestitures, McKinsey & Company, 2013

5 How to Use Supply Chain Design to Craft Successful M&A Activities, Llamasoft, 2014

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