

Case study: Cost Model Review & SKU Profitability Analysis

Client: Contract Manufacturer
Project : Project Execution

Background and Activities

- Operational diligence assignment, \$100mn food manufacturer
- Single digit GM% business
- Extremely high labor and overhead variances each month vs standard (GM% only half of standard GM%)
- PE buyer asked Saphineia to identify sources of low GM% and to estimate profitability by SKU
- Saphineia reviewed product costing model and costing process; analyzed run performance and scrap losses; studied variances

Benefits

- ✓ More accurate product costing going forward
- ✓ Better understanding of where business makes and loses money
- ✓ Provided PE buyer with valuable out-of-the gate value-creation opportunities

Saphineia's Findings

- Identified several flaws in costing model:
 - Underestimated Labor & OH cost per hour due to unrealistic utilization assumptions
 - Freight and storage costs were not properly included in standard costs
 - High levels of excess scrap vs standard
 - Did not achieve standard run speeds
- As a result, over 100% of its adjusted gross profit was generated by just 10% of SKUs; remaining SKUs rest lost money in aggregate

Saphineia's Recommendations

- Helped buyer and target fix flaws in costing model
- Encouraged target to update standard run speeds and scrap assumptions based on actual shop-floor performance

