Hansson’s Private Label

Group 6

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Overview

- Introduction & Company Background
- Deliverables
- Expansion Objective
- Financials
- Potential Risks
- Analysis (APV, WACC, etc.)
- Recommendations

Introduction

- HPL started in 1992; bought by Tucker Hansson, CEO.
- HPL was bought for $42 million.
  - **Private savings**: $25 million **Debt**: $17 million.
- HPL's products: soap, shampoo, mouthwash, shaving cream, and sunscreen.
- HPL's focus has been manufacturing efficiency, expense management, and customer service.

Hansson's Background

- Partners with supermarkets, drug stores, and mass merchants
- HPL is also known for being a conservative company:
  - By never exceeding their capacity. Any new facility has to operate a least 60% of capacity utilization.
  - Maintains modest level of debt to avoid risk of financial distress.

HPL's Mission

"To be a leading provider of high-quality label personal care products to America's leading retailers."

Analysis Overview

- Team Proposal Led by Executive VP of Marketing, Robert Gates
- Personal Care Industry
- Financial Analysis using WACC, APV, Sensitivity Analysis
- Depreciation Method: MACRS

Deliverables

- Recommendations to CFO Sheila Dowling, Robert Gates, and Tucker Hansson.
- Industry breakdown with Benchmark comparison.
- Hansson's position in the industry.
- Evaluate Robert Gates assumptions.

Expansion Objectives

- Increase production capacity to meet a large customer's demand through a 3-year contract.
- Funds (50M) will be raised via Debt Financing at an estimated after-tax cost of debt of **4.65%**.
- Grow relationships with our largest customer.
- Unit volumes are expected to continue rising at **100 bps** annually, followed by a price increase of **170 bps**.

Financials

Below are the company's financial ratios for 2007:

- Current Ratio: 2.85x
- Coverage Ratio: 20.42x
- Quick Ratio: 1.69x
- Inventory Turnover: 8.64x
- Return on Assets: 10.11%
- Debt-to-Assets: 29.65%

Potential Risks & Unknowns

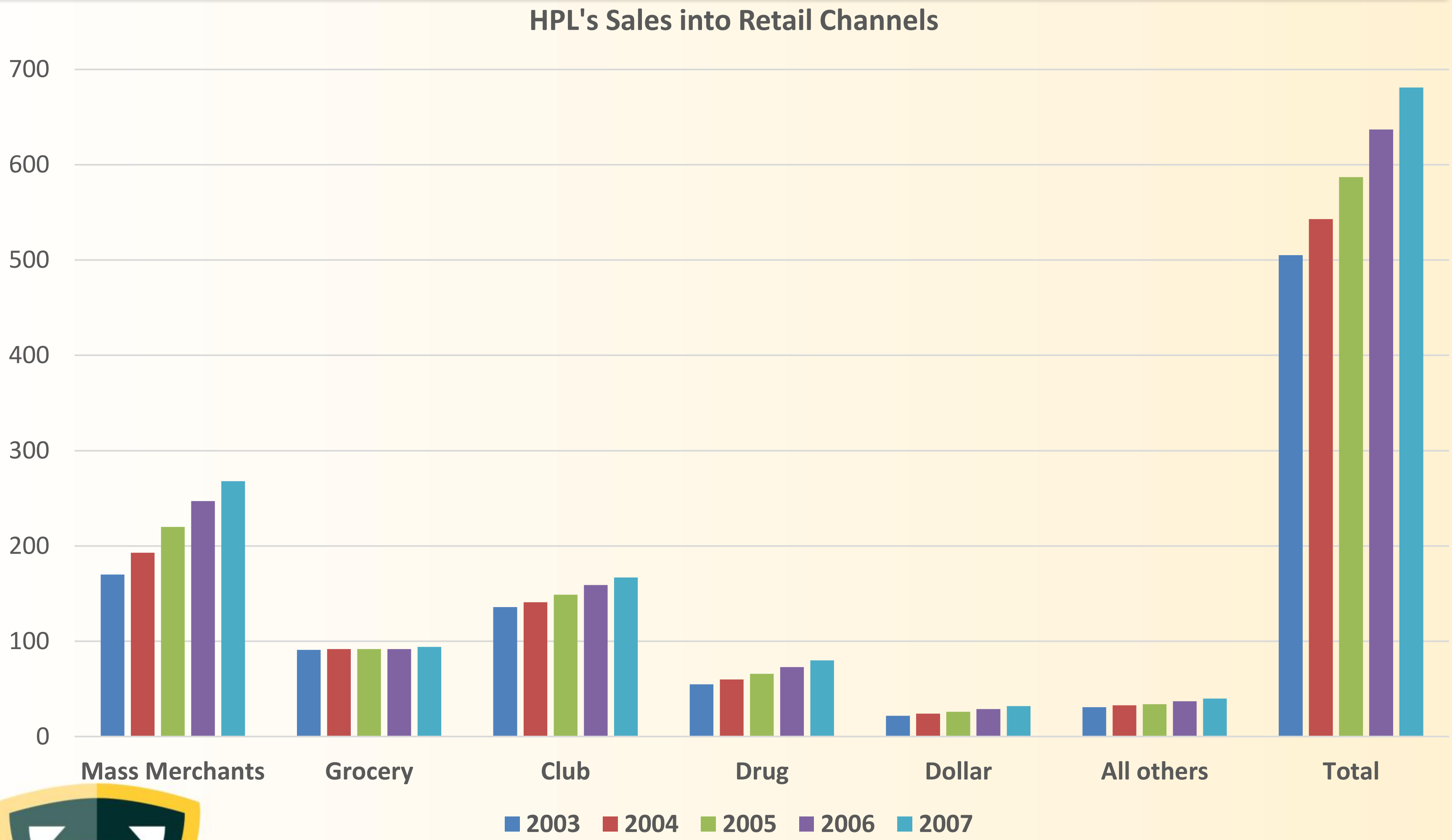
- Will the customer extend after the 3-year contract?
- Risk of Financial Distress
  - Double the Debt
  - Concentration of Hansson's wealth into a single non-diversified investment.
  - Increasing fixed costs (such as interest expenses).
- Are we guaranteed more of the limited shelf-space after increasing our production capacity?
- Our high Cash Conversion Cycle (~54).

HPL Revenue Segment

- Steady revenue growth.
- Increase of 34.87% from 2003 to 2007.
- Mass Merchants and Club account for 64% of total sales.

Sales in (US$ millions)					
Channel	**2003**	**2004**	**2005**	**2006**	**2007**
Mass Merchants	170	193	220	247	268
Grocery	91	92	92	92	94
Club	136	141	149	159	167
Drug	55	60	66	73	80
Dollar	22	24	26	29	32
All others	31	33	34	37	40
Total	**$505**	**$543**	**$587**	**$637**	**$681**

HPL Market Segments



Industry Analysis

- **Comps**

Company:	**Market Value**	**Net Debt**	**Enterprise Value**	**Equity Beta**	**Revenue**	**EBITDA**	**EBIT**	**Net Income**	**Book Value**
Cathleen Sinclair	298.9	1,329.6	1,628.5	2.22	1,346.8	255.3	163.4	21.5	(1,112.8)
General Health & Beauty	319.3	63.1	382.4	1.95	446.1	61.9	51.9	23.8	204.2
Women's Care Company	498.6	55.3	553.9	1.14	397.3	52.7	49.3	77.0	43.7
Skin Care Enterprises	1,204.2	371.9	1,576.1	1.35	1,247.6	155.8	125.4	65.3	316.2
Hansson Private Label	**593.2**	**54.8**	**648.0**	**1.20**	**680.7**	**73.5**	**67.4**	**38.5**	**267.9**

Benchmark Comparison

Company:	EBITDA	EBIT	Earnings	Revenue	EBITDA	EBIT	P/E	P/B
Cathleen Sinclair	19.0%	12.1%	1.6%	1.2x	6.4x	10.0x	13.9x	NM
General Health & Beauty	13.9%	11.6%	5.3%	0.9x	6.2x	7.4x	13.4x	1.6x
Women's Care Company	13.3%	12.4%	19.4%	1.4x	10.5x	11.2x	6.5x	11.4x
Skin Care Enterprises	12.5%	10.1%	5.2%	1.3x	10.1x	12.6x	18.4x	3.8x
Average	**14.6%**	**11.6%**	**7.9%**	**1.2x**	**8.3x**	**10.3x**	**13.1x**	**5.6x**
Median	**13.6%**	**11.9%**	**5.3%**	**1.2x**	**8.2x**	**10.6%**	**13.7%**	**3.8%**
Hansson Private Label	**10.8%**	**9.9%**	**5.7%**	**1.0x**	**8.8x**	**9.6x**	**15.4x**	**2.2x**

	2016 Y	2017 Y	Current	2018 Y Est	2019 Y Est
12 Months Ending	12/30/2016	12/29/2017	07/18/2018	12/29/2018	12/29/2019
Valuation Metrics					
Price/Earnings	20.56	21.70	21.31	17.62	15.97
Price/Earnings, Positi...	19.66	21.48	21.07	17.60	15.96
Price/Earnings before...	23.37	23.92	23.80		
Price/Book Value	2.93	3.27	3.39	3.23	2.98
EV/Sales	2.31	2.53	2.56	2.43	2.32
EV/EBIT	17.89	18.88	19.22		
EV/EBITDA	12.40	13.23	13.57	11.59	10.75
Dividend Yield	2.09	1.89	1.84	1.92	2.07
Fundamentals					
Gross Margin	33.59	33.72	33.65		
Operating Margin	12.77	13.83	13.74		
Profit Margin	8.87	9.19	9.49		
Return on Assets	2.73	2.88	3.03	3.56	4.32
Return on Equity	13.12	13.64	14.35	18.58	19.84

* Bloomberg Terminal

Expansion Project

- Robert Gates recommendation

$ in Millions **Cost Components:**	**Amount**	**Est. Life**	**Depr'**	**%** **Maintenance**	**Cost of** **Maintenance**
Facility Expansion	$10,000	20	500	0	$500
Manufacturing Equipment	20,000	10yrs.	2,000	5.0%	1,000
Packaging Equipment	15,000	10yrs.	1,500	5.0%	750
Working Capital (1)	12,817			0.0%	
Total Investment	**$57,817**		**$4,000**		**$2,250**

Expansion Project

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	-	84,960	93,881	103,124	112,700	122,618	132,887	135,545	138,256	141,021	143,841
Less: Raw Materials	-	(45,120)	(49,369)	(53,698)	(58,109)	(62,603)	(67,181)	(67,852)	(68,531)	(69,216)	(69,908)
Less: Labor	-	(18,640)	(20,233)	(22,842)	(25,255)	(28,175)	(30,888)	(31,970)	(33,089)	(34,247)	(35,445)
Less: Manufacturing Overhead	-	(3,600)	(3,708)	(3,819)	(3,934)	(4,052)	(4,173)	(4,299)	(4,428)	(4,560)	(4,697)
Less: Maintence Expense	-	(2,250)	(2,318)	(2,387)	(2,459)	(2,532)	(2,608)	(2,687)	(2,767)	(2,850)	(2,936)
Less: SG&A	-	(6,594)	(7,286)	(8,004)	(8,747)	(9,517)	(10,314)	(10,520)	(10,730)	(10,945)	(11,164)
Less: Depreciation	-	(4,000)	(4,000)	(4,000)	(4,000)	(4,000)	(4,000)	(4,000)	(4,000)	(4,000)	(4,000)
EBIT	**-**	**4,756**	**6,967**	**8,374**	**10,197**	**11,739**	**13,723**	**14,218**	**14,711**	**15,202**	**15,691**
Less: Taxes	-	1,902	2,786	3,349	4,078	4,694	5,487	5,685	5,883	6,079	6,274
NOPAT/EBIAT	**-**	**2,854**	**4,181**	**5,025**	**6,120**	**7,045**	**8,235**	**8,532**	**8,828**	**9,123**	**9,416**
Add: Depreciation	-	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000
Less: Change in NWC	-	(12,672)	(1,452)	(1,421)	(1,507)	(1,528)	(1,618)	(417)	(424)	(432)	21,471
Less: Capital Expenditures	($45,000)	-	-	-	-	-	-	-	-	-	-
Less: Excess Cash	-	-	-	-	-	-	-	-	-	-	-
Unlevered Free Cash Flow (FCF)	**(45,000)**	**(5,818)**	**6,729**	**7,604**	**8,613**	**9,517**	**10,617**	**12,115**	**12,404**	**12,692**	**34,887**
Discount Factor	1	0.91	0.84	0.77	0.70	0.64	0.59	0.54	0.49	0.45	0.41
Discounted Free Cash Flow	($45,000)	($5,322)	$5,632	$5,821	$6,032	$6,097	$6,222	$6,496	$6,084	$5,695	$14,320
Cumulative DCF	($45,000)	($50,322)	($44,690)	($38,869)	($32,837)	($26,740)	($20,517)	($14,022)	($7,938)	($2,243)	$12,076
Sum of Discounted Cash Flow	$12,076										
Cost if Capital (Opportunity Cost	9.3%										

Go/No-Go Commitment

Value Analysis

	2008	2009	2010	2011
Revenue	**-**	**84,960**	**93,881**	**103,124**
Less: Raw Materials	-	(45,120)	(49,369)	(53,698)
Less: Labor	-	(18,640)	(20,233)	(22,842)
Less: Manufacturing Overhead	-	(3,600)	(3,708)	(3,819)
Less: Maintenance Expense	-	(2,250)	(2,318)	(2,387)
Less: SG&A	-	(6,594)	(7,286)	(8,004)
Less: Depreciation	-	(4,000)	(4,000)	(4,000)
EBIT	**-**	**4,756**	**6,967**	**8,374**
Less: Taxes	-	1,902	2,786	3,349
NOPAT a/k/a EBIAT	**-**	**2,854**	**4,181**	**5,025**
Add: Depreciation	-	4,000	4,000	4,000
Less: Change in NWC	-	(12,672)	(1,452)	14,123
Less: Capital Expenditures	(45,000)	-	-	-
Less: Excess Cash	-	-	-	-
Unlevered Free Cash Flow (FCF)	**(45,000)**	**(5,818)**	**6,729**	**23,149**

Cost of Capital (Opportunity Cost)	9.3%
NPV of Future Cash Flows	$18,035
Less: Today's Investment	(45,000)
Project Valuation	($26,965)
Go/No-Go?	**NO GO!**

Weighted Average Cost of Capital

Company:	Debt/ Value	Debt/ Equity	Equity Beta	Debt Beta	Asset Beta
Cathleen Sinclair	81.6%	444.9%	2.22	0.00	0.60
General Health & Beauty	16.5%	19.8%	1.95	0.00	1.74
Women's Care Company	10.0%	11.1%	1.14	0.00	1.07
Skin Care Enterprises	23.6%	30.9%	1.35	0.00	1.14
Average	**32.9%**	**49.1%**	**1.67**	**0.00**	**1.14**

Debt/ Value	Debt/ Equity	Asset Beta	Equity Beta	Cost of Equity	Cost of Debt	WACC
0.0%	0.0%	1.14	1.14	9.44%	7.75%	9.44%
5.0%	5.3%	1.14	1.17	9.62%	7.75%	9.38%
10.0%	11.1%	1.14	1.21	9.82%	7.75%	9.31%
15.0%	17.6%	1.14	1.26	10.05%	7.75%	9.24%
20.0%	25.0%	1.14	1.31	10.30%	7.75%	9.17%
25.0%	33.3%	1.14	1.37	10.58%	7.75%	9.10%

Cost of Equity	**9.82%**

Weighted Average Cost of Capital

- **CAPM**

Debt	**Amt**	**Rate**	**Weights**
LT Debt	54.8	2.8%	48.54%
ST Debt	58.1	2.28%	51.46%
Total	**112.9**		**100%**

Debt	$112.9	47%	2.5%
Equity	$267.9	53%	11.6%
Total Capital	**$380.8**	**100%**	

rd = 2.5%

WACC= 6.9%

WACC= (we*re)+(wd*rd*(1-t))

Cost of Equity	
Capital Asset Pricing Model (CAPM)	
re =	**11.6%**
rf	2.69%
Rm	10.14%
MRP	7.45%
Beta	1.20

re rf + MRP (market risk premium) + individual issue premium

re rf + B*(rm - rf)

Adjusted Present Value

Cash Inflows:		$64,361
Cash Costs (82% of Sales):	$	52,776
Initial Investment	$	(45,000)
Tc:		40.0%
R_0		20.0%
Debt Financing	$	11,000
		Cash Flows
Cash Inflows		$64,361
Cash Costs	$	(52,776)
Operating Income	$	11,585
Corporate Taxes	$	(4,634)
Unlevered Cash Flow	$	6,951
Divide by R_0		20.0%
Present Value of Cash Flo\	$	34,754
Initial Investment	$	(45,000)
NPV	**$**	**(10,246)**
B	$	11,000
T_C	$	0
NPVF	$	4,400
APV	**$**	**(5,846)**

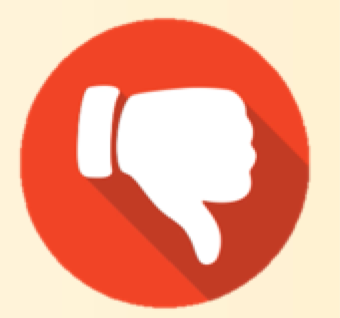
Robert Gates Recommendation

- Restructure for a lower discount rate, for a positive NPV to avoid cannibalizing the company.
- Restructure the terms of the commitment for a longer period.
- Utilize more leverage.

Go/No-Go Recommendation

No-Go

- Avoid deal.
- Continue with the current arrangements with largest retailer.
- Will impact HPL largest revenue stream negatively.

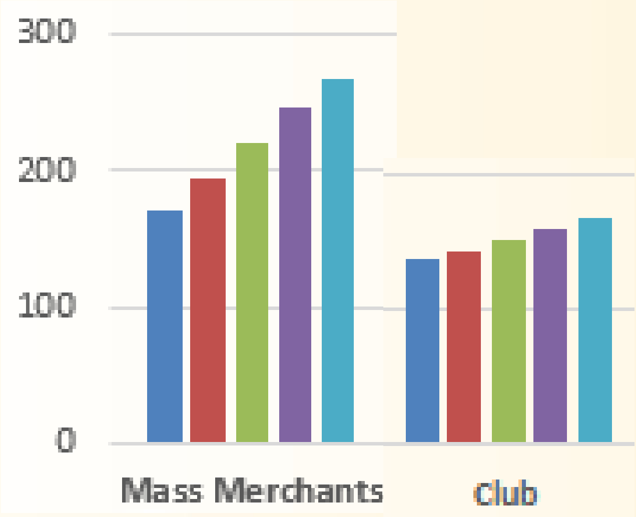


Expansion Recommendation

- Pursue project under current agreement.
- DCF demonstrates largest upside with $12,076.
- Positive Free Cash Flows starting in year 2010.

Hansson Recommendation

- Continue revenue growth with new product offerings.
- Focus on products that have quick DSO in Mass Merchants and Club retailers.
- Follow Discounted Cash Flow statement for the expansion project.



To Sum Up

- Highly cyclical industry.
- Industry breakdown of Hansson's Private Label and position.
- Case study highlights:
  – Financial statements
  – Key ratios
  – Valuation of each project
  – Recommendations

Any Questions or Comments?

Thank you