American Bronze (A)

This case serves solely as a basis for class discussion. Some of the information in this document is fictionalized to preserve confidentiality.

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Background

In the spring of 2008, the evening news seemed to repeat the same messages over and over: markets were in peril, home prices were in free fall, and consumer confidence was shaken to the core. Mike Lewis sat at his desk well into the evening and scrolled through his opportunity pipeline. He saw a lot of companies that had posted good results through 2007, but were these end markets getting pummeled in 2008? Remaining committed to finding a stable, profitable manufacturing or engineering services company, Mike wondered: is there such a thing?

Choosing the ETA Path

Mike Lewis

Growing up, doing yard work and fixing things around the house with his parents was just a way of life for Mike, so parlaying these skills into a BS in mechanical engineering at the University of Florida seemed like a natural progression. After graduation, Mike was recruited to join GE Energy's Operations Management Leadership Program where he held positions as a project manager, shop floor supervisor, and sourcing commodity leader. He subsequently became a Lean Six Sigma Black Belt and earned the opportunity to run a $10 million pipeline inspection services P&L within GE Oil & Gas.

Mike's proven success at GE helped to secure his acceptance to a top graduate school program. Mike had applied to the highly-selective MMM program at Northwestern University which was a combined Master of Engineering Management and MBA from the Kellogg School of Management.

In his final year at Kellogg, Mike worked part-time for a Chicago-based private equity firm where he helped portfolio companies with lean process improvements and evaluated prospective deals.

The Search

During his time at Kellogg, Mike encountered the entrepreneurship through acquisition model and was struck by the unique opportunity to leverage his operating experience and freshly acquired Masters' degrees. Although he was unaware of search funds prior to business school, this was the exact opportunity that led him to get his MBA. During his second year at Kellogg, in the spring of 2007, Mike formed his search fund.

Mike focused his search on founder-run manufacturing or engineering service businesses in need of a succession plan. Mike believed he could employ his engineering skills and manufacturing experience to win immediate credibility with employees and grow a business. He identified and evaluated several potential businesses, and in 2008, Mike found a prime target in American Bronze.

Company

Overview

Founded in 1935 and located in Chicago, IL, American Bronze was a leading manufacturer of metal religious products used primarily by churches. John Rogers, 100% owner of American Bronze, took over the business from his father in 1971 and built it into a leading supplier of religious products. John was in his 70's and lived full-time in Naples, FL with his wife Betty, who was 60.

Products, sold under a recognizable brand name, included candlesticks, tabernacles, sanctuary lamps, holy water fonts, holy water pots and sprinklers, incense censers and boats, candelabra, Stations of the Cross, and bells (**Exhibit 1**). The products were made primarily from bronze or brass using proprietary company-owned patterns. American Bronze owned the molds, patterns, and dies for over 5,500 proprietary products. For over 70 years, the Company had been a premier producer of high-end metal religious products and was known for quality and reliable supply.

Customers & Go-to-Market

American Bronze sold via a network of approximately 250 church-goods dealers who supply to churches throughout the United States and Canada. The company had no significant customer concentration (the largest customer in 2007 accounted for 3.3% of sales), and the customer base tended to be extremely loyal (**Exhibit 2**). Most of its customers were family-owned and -operated, and relationships within the industry tended to be stable and long-lasting. American Bronze enjoyed a high level of repeat business: 96% of customers with more than $5,000 of purchases in 2006 were customers in 2007.

Management & Employees

American Bronze had a non-union workforce of 19 full-time and 3 part-time employees, with an average tenure of 21 years. The foreman running the factory had been with the company for 51 years and wanted to retire, and the owners ran the business as absentee owners from Florida.

Financial Overview

Historically, American Bronze had a track record of stable revenues and strong margins. For the twelve months ended June 2008, the Company generated $3.1 million and $0.8 million in Revenue and EBITDA, respectively, for a 27.0% margin (**Exhibit 3**).

Industry

Overview

Although American Bronze's customers were church-goods dealers, the end consumers for the Company's products were churches. American Bronze serviced U.S. and Canadian churches who reported $34 billion in total income for 2006, a slight increase over 2005, driven by a 4.1% increase in per capita giving, according to the Yearbook of American & Canadian Churches (2008). Donations per church member remained relatively steady through multiple economic cycles, indicating that the primary revenue stream in the end market was stable. Mike and his investors also felt reassured by the relatively low cyclicality of church expenditures in the past (**Exhibit 4**).

Competition

With its 73-year-old brand and over 5,500 SKU's, American Bronze occupied a defensible leadership position as a premier supplier of metal church goods with customers who greatly valued tradition. Products were not mass manufactured; they were often customized or made per order since this was a low-volume, high-customization business. The Company's primary competitors included Regal Empire Bronze Corporation, Koley's Inc., Sudbury Brass, Adrian Hamers, and a few other small manufacturers. All were family owned "mom and pop" manufacturers focused on making metal church goods in the United States.

Competitors went to market through the same distributors as American Bronze. Competition was friendly and included arrangements to buy and sell some parts from competitors. Historically, American Bronze and its main competitors raised prices in the fall of each year and observed few efforts to dramatically undercut pricing.

The Opportunity

American Bronze exhibited many of the characteristics of an attractive target that Mike had identified at the beginning of his search, and based on his diligence, he saw an opportunity to invest in a high-quality, niche business with stable revenue and a highly-defensible industry position. The Company's low customer concentration and a resilient track record through macroeconomic cycles further underscored the strength of the platform. Furthermore, candlesticks and other metal items represented a fairly low share of wallet for churches, so American Bronze's products were unlikely to be the focal point for cost-cutting in times of economic hardship.

For Mike, American Bronze's largely absent ownership group and foreman nearing retirement presented a unique opportunity to bring his operational expertise to the business. Despite historically strong margins, the Company's business practices were highly-unsophisticated. American Bronze carried excessive inventory, did not track production or worker productivity, had no website, and did very little to promote its goods and services. All company records were kept on notecards instead of electronically, financial reporting was done by hand, no one used Microsoft Office, and only one person used email in the company. After the acquisition, excess inventory could be sold off for immediate cash generation, and crucially, Mike believed that implementation of Lean Manufacturing along with basic operating improvements like the introduction of electronic record keeping and Microsoft Excel could significantly improve productivity.

Mike also identified several potential avenues to stimulate revenue growth, including promoting refurbishment services to leverage the Company's installed base of customers, improving promotional materials and dealer support, developing new products, and expanding distribution (including internationally).

Finally, Mike believed there was an opportunity to grow the business through the acquisition of American Bronze's "mom and pop" competitors as existing management teams grew older and looked for an opportunity to exit.

The Deal

In March 2008, Mike approached John Rogers with a letter of intent to acquire American Bronze. The proposal included both the purchase of the assets and real estate of American Bronze (i.e., the Company's 29,000 square foot manufacturing facility). Mike and the seller entered into an exclusivity agreement, which allowed Mike time to conclude his diligence efforts.

Mike identified a few key areas of focus in diligence. First, Mike believed that the risk of cheap "knockoff" products from China potentially threatened American Bronze's market positioning. If competitors imported these cheaper products, American Bronze could quickly lose share and customers. However, Mike found that American Bronze's low-volume, highly-customized products provided insulation against this risk. The tooling required to make these products was cost prohibitive to reproduce for such a niche market, and customers generally preferred their religious products to be made in the USA over China.

Second, Mike needed to validate American Bronze's market share. Given the lack of market research available and the highly-fragmented nature of the market, no authority on market share existed. To solve this problem, Mike painstakingly combed customer catalogs and spoke directly to customers. In doing so, he was able to verify the abundance of American Bronze products relative to competitors and get comfortable with the Company's market share.

Finally, since Mike intended to purchase the manufacturing facility, state and federal environmental liability was a key area of focus. He hired a specialized consulting firm to review the company's safety practices which identified several minor updates that the seller committed to completing prior to closing. Mike also secured an agreement that stipulated that the sellers would complete (i.e. fund) the requisite real estate environmental diligence. The real estate diligence was more involved than originally anticipated which caused the sellers to complete an asbestos survey and Phase I and Phase II environmental studies with acceptable results.

The extensive diligence had delayed closing, but Mike and his investors felt the extra time and precautions were a worthwhile investment as diligence wrapped up and he prepared to close the acquisition. As Mike completed his diligence, he began structuring the acquisition. The proposed capital structure included a revolving credit facility, term loan, seller note, and equity from Mike's investors. Mike would acquire American Bronze $4.9 million, comprised of $4.5 million in cash at closing and the remaining $400,000 in the form of a seller note.

Market Turmoil

On September 15, 2008, Lehman Brothers filed for bankruptcy, and credit markets froze. Suddenly, Mike's lenders told him that his original deal was no longer possible. Mike, confident he had found the right business to acquire, immediately went to work to negotiate a new deal with his lender that would still be acceptable to the sellers and his investors.

After a series of negotiations, Mike struck a deal with his lender, the sellers, and his investors that reduced the total borrowing by leasing the facility instead of buying the real estate. As an added benefit, this provided the Company with more flexibility to determine its long-term facility needs. An updated letter of intent was signed, and the seller agreed to complete the remaining requirements for compliance with environmental laws and regulations.

Ultimately, Mike was able to restructure the transaction. The new structure included $3 million cash (comprised of the term loan, partially funded revolver, and investor equity) at closing plus $1 million in the form of a seller note **(Exhibit 5**). In total, Mike agreed to pay $4 million or 4.8x June 2008 TTM EBITDA. Finally, in December 2008, after several months of diligence and multiple transaction structures, Mike closed on the acquisition of American Bronze.

The Future

In January 2009, as Mike drove the Rogers family to the airport, he pondered on last year's ups and downs. Mike had been through a stressful 2008. Searching for a good business was emotionally draining. The deal process, which already tends to be stressful, felt particularly difficult because of the fear and uncertainty that had infected credit markets.

As his thoughts shifted to the future, Mike felt truly energized by the opportunities to improve the operations of American Bronze, the perfect, insulated business to own during what seemed to be an economic calamity. He was excited to finally get to work. The only question remaining was where to start.

Exhibits

Exhibit 1 – Top Products

2007's Top 20 Product Category Sales

	2005		2006		2007	
Product Category	$	%	$	%	$	%
Candlesticks	630,010	22.2%	626,897	20.9%	797,124	25.2%
Tabernacles	260,857	9.2%	308,981	10.3%	334,823	10.6%
Refinishing	221,732	7.8%	266,753	8.9%	178,112	5.6%
Lamps	162,127	5.7%	177,223	5.9%	176,530	5.6%
Crucifixes	176,731	6.2%	145,479	4.8%	169,363	5.4%
Fonts	146,873	5.2%	144,628	4.8%	147,520	4.7%
Censers & Boats	113,163	4.0%	111,687	3.7%	102,546	3.2%
Burners	93,836	3.3%	101,786	3.4%	99,839	3.2%
Holy Water Pots & Sprinklers	69,448	2.4%	76,125	2.5%	83,372	2.6%
Candelabras	58,049	2.0%	67,958	2.3%	72,908	2.3%
Bells	63,969	2.3%	65,466	2.2%	70,215	2.2%
Crosses	49,689	1.8%	38,042	1.3%	68,429	2.2%
Stations of the Cross	41,824	1.5%	66,739	2.2%	61,202	1.9%
Votive Stands	45,619	1.6%	44,214	1.5%	47,122	1.5%
Sockets	45,141	1.6%	42,819	1.4%	46,198	1.5%
Stands	49,448	1.7%	48,162	1.6%	40,804	1.3%
Missal Stands	31,366	1.1%	29,258	1.0%	32,886	1.0%
Holy Water Reservoirs	17,158	0.6%	38,704	1.3%	32,512	1.0%
Miscellaneous	69,147	2.4%	34,100	1.1%	31,685	1.0%
Candle Tubes & Holders	39,080	1.4%	40,605	1.4%	30,172	1.0%
Sum of Top 20	2,385,267	84.1%	2,475,627	82.5%	2,623,361	82.9%

Exhibit 2 –Top Customers

	2007's Top 25 Customer Sales					
	2005		2006		2007	
	$	%	$	%	$	%
Customer 1	103,563	3.7%	106,717	3.6%	102,983	3.3%
Customer 2	111,547	3.9%	103,545	3.4%	93,538	3.0%
Customer 3	101,439	3.6%	91,164	3.0%	90,129	2.8%
Customer 4	79,012	2.8%	92,536	3.1%	86,999	2.8%
Customer 5	64,732	2.3%	111,621	3.7%	84,633	2.7%
Customer 6	45,977	1.6%	27,435	0.9%	71,961	2.3%
Customer 7	60,323	2.1%	62,163	2.1%	71,884	2.3%
Customer 8	85,463	3.0%	48,301	1.6%	70,168	2.2%
Customer 9	100,288	3.5%	79,228	2.6%	68,964	2.2%
Customer 10	33,977	1.2%	79,417	2.6%	66,456	2.1%
Customer 11	36,055	1.3%	37,348	1.2%	66,143	2.1%
Customer 12	80,484	2.8%	52,962	1.8%	61,542	1.9%
Customer 13	69,702	2.5%	72,705	2.4%	59,841	1.9%
Customer 14	47,822	1.7%	43,324	1.4%	58,355	1.8%
Customer 15	44,957	1.6%	59,634	2.0%	50,886	1.6%
Customer 16	34,116	1.2%	30,130	1.0%	50,508	1.6%
Customer 17	47,227	1.7%	47,493	1.6%	49,389	1.6%
Customer 18	49,661	1.8%	63,767	2.1%	46,873	1.5%
Customer 19	-	0.0%	-	0.0%	45,309	1.4%
Customer 20	11,104	0.4%	37,234	1.2%	44,288	1.4%
Customer 21	35,301	1.2%	50,192	1.7%	40,281	1.3%
Customer 22	13,484	0.5%	26,811	0.9%	39,508	1.2%
Customer 23	26,778	0.9%	42,061	1.4%	39,204	1.2%
Customer 24	30,829	1.1%	23,491	0.8%	39,170	1.2%
Customer 25	34,975	1.2%	35,701	1.2%	38,813	1.2%
Sum of top 25	1,348,817	47.5%	1,424,979	47.5%	1,537,822	48.6%

Exhibit 3 – Historical Financials

Historical Financial Information

($ in thousands)

	Fiscal Year Ending December 31,				
	2004	2005	2006	2007	Jun 08 TTM
Revenue	2,708	2,837	3,002	3,163	3,078
COGS (1)	1,482	1,671	1,767	1,930	1,837
Gross Profit	1,226	1,166	1,235	1,233	1,241
Op. Expense (1)	398	400	465	513	438
EBITDA	828	766	770	720	803
Total Adjustments	-	66	45	105	27
Adjusted EBITDA	828	832	815	825	830
Revenue Growth	n/a	4.8%	5.8%	5.4%	-2.7%
Gross Profit %	45.3%	41.1%	41.1%	39.0%	40.3%
Adj. EBITDA %	30.6%	29.3%	27.1%	26.1%	27.0%

(1) Depreciation & amortization are excluded from COGS & SG&A respectively

Exhibit 4 – Sales vs. Church Giving per Member

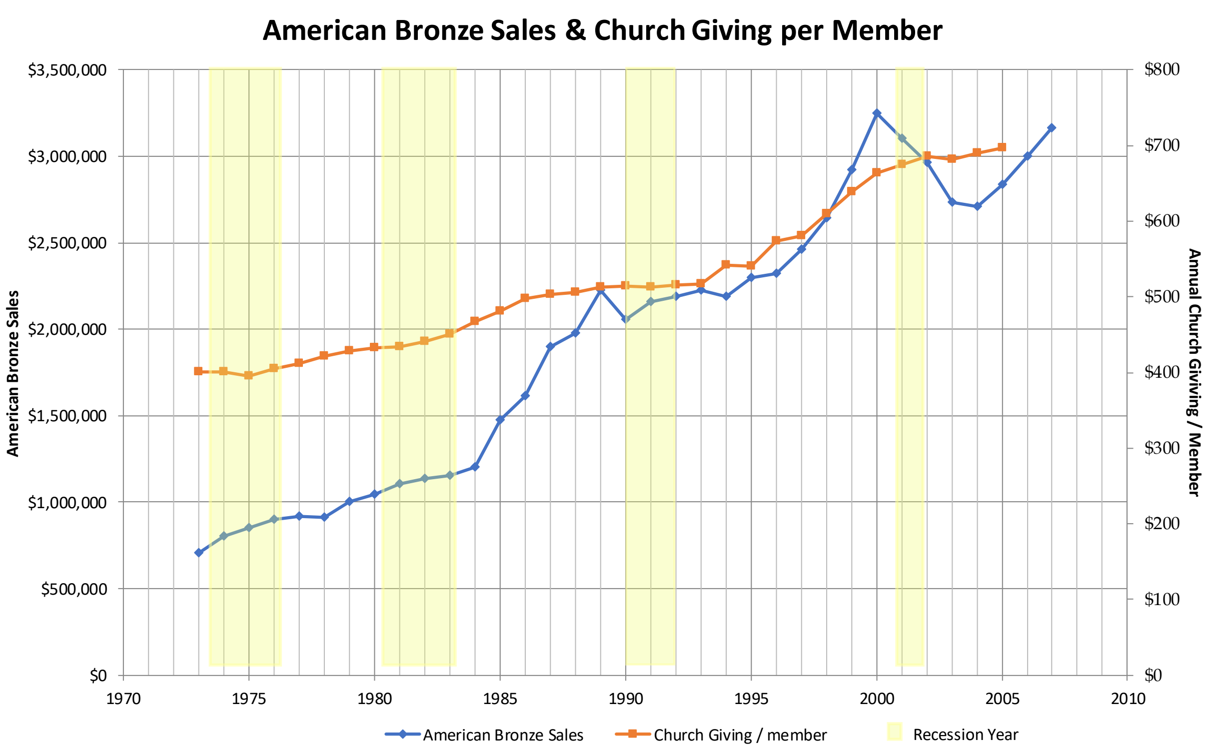

Exhibit 5 – Transaction Structure

Sources & Uses - Revised Offer

($000s)

Sources		**Uses**	
Revolver[1]	$190	Purchase Assets	$3,000
Term Loan	1,000	Seller Note[2]	1,000
Seller Note[2]	1,000	Fees & Expenses	225
Remaining Search Captial	135		
Investor Equity	1,900		
Total Sources	**$4,225**	**Total Uses**	**$4,225**

(1) $500,000 revolving credit facility, of which $190,000 drawn at closing.
(2) 5-year, 7% cash pay unsecured, subordinated note.

