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DEAL MECHANIC

Building value

WATERFORD WEDGWOOD/ KPS CAPITAL PARTNERS

Crystal clear

Waterford Wedgwood, the famous china and crystal company, almost went out of existence in 2009. Three years later it seems to be thriving under its new owner, New York-based turnaround firm KPS. James Taylor *talks to the principals involved*

"I've spent 22 years – that's half my life – immersed in turning around troubled or underperforming businesses. And I can tell you unequivocally: I have never seen a company that was as poorly run as Waterford Wedgwood. In many cases with a turnaround you have a marketing problem, or a strategic problem, or maybe a combination of both. This was a case where every single aspect of the business was broken."

This is how Mike Psaros, the managing partner of New York-based KPS Capital Partners, describes the company he found when, in early 2009, his firm agreed to buy some of Waterford Wedgwood's assets from the receiver in Ireland (a deal that ended up spanning ten separate legal jurisdictions).

The aim of this column is to take a detailed look at examples of private equity transforming companies for the better. And in 2009, there were few companies in greater need of transformation than Waterford Wedgwood. The Irish company clearly had some famous brands: it makes Wedgwood and Royal Doulton china, as well as Waterford crystal. But financially, it looked like a basket case: after years in the red, it collapsed into receivership in early 2009 with debts of more than a billion dollars. At the time, it was making $450 million in revenue a year – but losing nearly $100 million, even before interest payments. Various private equity firms had looked at it; not one had submitted a bid.

However KPS – which Psaros describes as "a hardcore, full-body-contact, operations-driven turnaround firm" – saw potential where others did not. "The big picture was: you had three magic brand names, each with a 200-year heritage, and you had spectacular products that were selling in 80 countries around the world – despite it being the worst-run business I'd encountered in two decades. That really speaks to the power of the brands," says Psaros.

Today, Waterford Wedgwood is a very different business. KPS won't give out specific profit numbers, but the company climbed back into the black in the very first year of the firm's ownership, and has been growing the bottom line steadily ever since. Its debt burden, which in 2009 stood at $1.1 billion, is now less than $50 million. KPS has cut more than $130 million of cost out of the business, while effectively doubling productivity thanks to a number of organizational changes and manufacturing improvements (and it was all done in-house, without the use of external consultants). Not bad for a basket case…

COST-CUTTING

It helped of course that WWRD, the holding company formed by KPS to buy the Waterford Wedgwood assets, started out free from the huge debt burden that had brought the old company down (it been spending $60 million a year on interest payments). By contrast, NewCo's only debt was a £50 million asset-backed loan facility from Bank of America to provide essential working capital (it's now even lower).

The WWRD workforce was also much smaller. When it went bust, the original company had employed about 6,600 people;

"It's almost impossible to explain how bad this company's cost structure was"

KPS offered jobs to about 3,600 of them (Psaros is very keen to emphasise that this doesn't mean KPS made 3,000 people redundant, since all 6,600 had already lost their jobs as part of the liquidation process). This clearly made a big difference to the company's cost base.

However, this headcount reduction – much of which was due to KPS deciding not to buy the company's loss-making retail operation – did not lead to a huge drop in output. In fact, by overhauling the structure of the company and boosting productivity, the new company was actually able to produce the same amount of stuff, but with far fewer staff.

One of the first things KPS had done on taking over the business was to appoint a new CEO, Pierre de Villemejane, who had already worked with the firm on the turnaround of technology business Speedline Technologies. It's easy to see why KPS wanted to work with him again: he made the fund a return of 15.5 times its invested capital in just three years. "Pierre spent the early part of his career at L'Oreal – so he understands manufacturing and logistics and distribution, but he also has the classic L'Oreal luxury goods marketing training. He was the perfect guy for the job," says Psaros.

"I've known KPS since 2003 and this is my second turnaround, so we have a great working relationship," de Villemejane tells *PEI*. "Whatever your equity structure, when you have this level of trust between a CEO and his board/ shareholder, that's the best you can hope for. KPS's business model is to be very lean in terms of people but they're very involved in the business; they trust what I do, and of course they're very involved in any major investment we make."

But while the new boss was primed for a challenge, he hadn't expected things to be quite so bad. "Everything was broken," says de Villemejane. "That's what shocked me at the beginning – the extent of the turnaround required. Everything had to be re-thought."

For instance, the four divisions of the business, previously independent, were combined into one. "It's almost impossible to explain how bad this company's cost structure was," scoffs Psaros. "There were four different manufacturing processes; four different marketing heads; four different sales forces… Every single area where there should have been one consolidated function, there was four. And all four brands were out in the market competing with each other."

Yet Psaros boasts that despite this internal overhaul, the company did not miss a single order during the transition process. In fact, he says: "[WWRD] is designing, manufacturing and selling the same amount of product as [Old Co] with half the amount of people. So the question I still wonder about to this day is: why was [Old Co] staffed in such an inefficient manner?"

Improving manufacturing productivity clearly played a big part. The company's factory in Indonesia is now, according to Psaros, "the most cost-effective plant for high quality bone china in the world." So what did KPS change, exactly? "Our operations team has spent an enormous amount of time on the shop floor in Indonesia. It's about worker training, manufacturing metrics, shop floor layout, product flow throughout the plant… And of course management."

KPS had decided not to buy the existing Waterford factory in Ireland from the receiver, on the grounds that it was no longer competitive (by the end, it was down to a single production line). However, recognising the need to have a base in Waterford, it persuaded the Irish government to pay for the construction of a new site – part factory, part showroom, part shop. KPS claims the new Waterford facility is now Ireland's second biggest tourist attraction, and attracted some 200,000 visitors last summer.

KPS and de Villemejane also overhauled Waterford Wedgwood's supply chain, and its distribution model. "The manner in which the product was distributed around the world was a disaster. It was handled too much; it was shipped to too many warehouses; the warehouses were in the wrong place… We literally had to start with blank piece of paper. How should this company distribute its products worldwide? That meant a new warehouse footprint, a new logistics provider, and new freight companies."

All told, KPS cut costs line by $130 million. Psaros couldn't say how much of this was people-related, but he stresses that it couldn't have been done without "attacking every single aspect of how the product is designed, manufactured, distributed and sold…There were hundreds of unique individual discrete actions taken to achieve [that saving], over an 18-month period."

EARLY OFFENSIVE

Gaining the trust of staff was clearly a challenge too; particularly in Ireland, where KPS took on a shrunken and demoralised work-force. "It was a very difficult time," de Villemejane admits. "When we took over there were all kinds of rumours about us dismantling the group and selling assets piecemeal… It took a good 12 months of high-profile measures to convince people that we were there to grow a portfolio of brands, not strip assets."

But although there were plenty of fires to fight, de Villemejane was already thinking about the next stage of the company's recovery. "Usually on KPS turnarounds we play defense first – so you do the turn, and then you play offense," says Psaros. "This was one of the rare occasions when Pierre started playing offense on the day we created the company."

The key to this was sorting out the company's outdated and badly targeted product range.

"One of the issues was a lack of focus on understanding the consumer," says Villemejane. "Because it had gigantic problems financially, the old management team didn't spend time thinking about what type of new products they needed to deliver to the next generation of consumers."

The first task was to reduce the number of products. "The old company was carrying tens of millions of dollars of excess inventory, largely associated with product that was manufactured but not properly test marketed to see whether there was consumer demand," says Psaros.

The second was to revitalize all three brands; so Waterford, Wedgewood and Royal Doulton are no longer mere tablewear, but "luxury home and lifestyle brands". Waterford and Wedgwood have become the premium aspirational ranges, while Royal Doulton is intended for a slightly younger, trendier audience. It has also relaunched Royal Albert, an English floral vintage china range.

With developed markets stagnant, the company is throwing resource at Asia, which now accounts for a third of its revenues. "We're on full attack in China," says Psaros. "We believe that within the next two or three years we can have 200 different locations there. It's going to be a huge growth market for us."

Hospitality will be, too, it hopes; it's already signed a deal with Emirates to supply fine china for its first and business class customers (supposedly the biggest such deal an airline has signed to date), and has just start building a specific team to exploit what it believes can be a big market opportunity.

Both Psaros and de Villemejane say they now wish they'd pushed their growth strategies harder, sooner. "It's difficult because you always want a little bit of continuity," admits the Frenchman. "But there are a couple of changes made over last two years that could have been done earlier."

Still, they're both clearly very proud of what KPS has done with Waterford Wedgwood. As Psaros puts it: "A 257-year old enterprise went into bankruptcy, and nobody wanted to touch it. Now look at where it's at today." The proof of the pudding will come when KPS sells the business – but it's hard to imagine this being anything less than a highly profitable exit. ■

DIAGNOSTIC: KEY FACTS

When it went into receivership in 2009, Waterford Wedgwood had debts of over $1 billion and was losing almost $100 million a year (even before its $60 million a year interest payments). It is now profitable and has less than $50 million of debt

Headcount is now 3,600, down from 6,600 – but without any drop in overall output

Costs have been cut by $130 million thanks to an organisational overhaul (whereby the company's four separate divisions were consolidated into one), an increase in manufacturing productivity, and an entirely new sourcing and distribution model

Opened a new factory in Waterford, Ireland (the old one had been closed down by the receiver) to make high-end, hand-made crystal. It's now a popular tourist attraction, with more than 200,000 visitors last summer

Repositioned and re-launched all three major brands – plus a fourth, Royal Albert

A third of its revenues now from Asia; it plans to increase its number of retail outlets in China from 30 to more than 200 in the next few years