

Avondale Perspective:
Understanding customer value;
driving profitable growth

Avondale News:
We are pleased to announce the
formation of Avondale Strategic
Partners

Avondale Connections:
More on Avondale’s practice

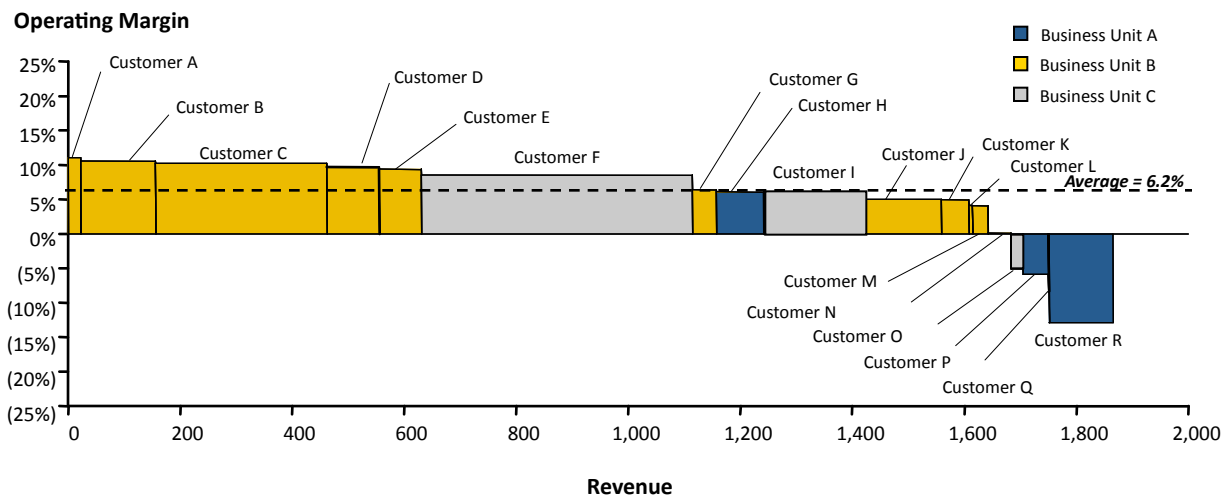
Avondale Perspective: Understanding Customer Value; Driving Profitable Growth

Many companies have more customer data than they know what to do with, and are not harnessing this rich data to its full extent. This means they are missing opportunities to improve profitability and attract and retain more profitable customers.

Any management team is likely to acknowledge the need to leverage customer data more effectively. Companies have a wide range of effective tools for basic data mining – understanding a customer’s revenue and gross margin contribution, for example. But many companies stop there.

What’s missing? You can’t identify the truly valuable opportunities in your core business until you understand the drivers of customer profitability at a more granular level. What is driving higher margins for certain customers? What is driving higher share of wallet among others? Answering these questions involves an understanding not just of past performance, but of the growth potential for each customer or segment.

Operating Profit by Customer

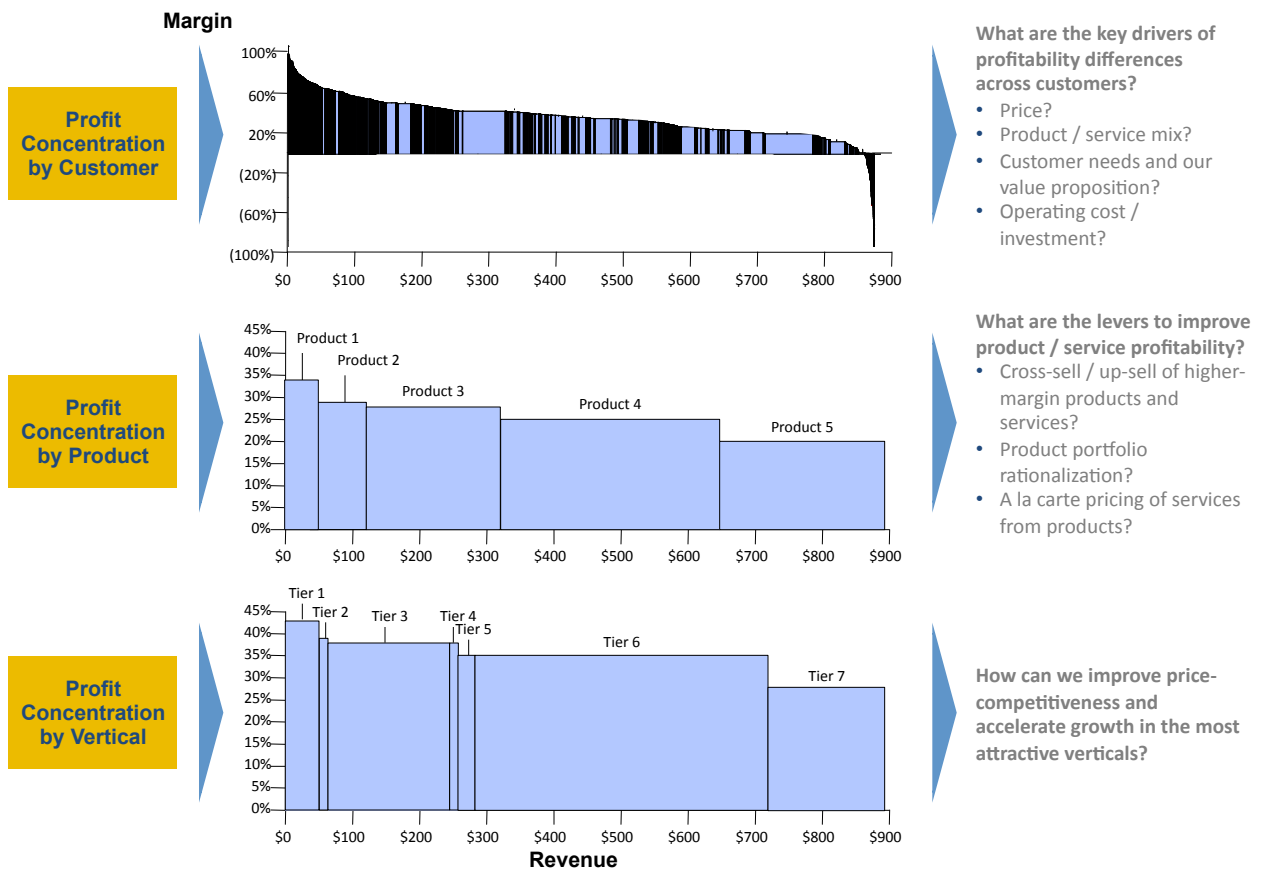


Creating a holistic view of customer profitability involves four key steps:

1. Calculate profitability at the most granular level, e.g., customer- and product-level profitability
 - Understand fully loaded profitability as well as variable contribution
 - Use activity-based costing where possible
2. Analyze customer data to determine the drivers of customer profitability
 - e.g., customer size, tenure, product mix, relative price, relative cost-to-serve
3. Develop a prioritized list of profitable growth and margin improvement that will collectively drive a step-change performance improvement
4. Execute those opportunities and continuously refine the view of profitability as well as evolving priorities

With this approach, managers can be confident they are maximizing the value of current customers and capturing the highest-value core business opportunities.

Illustrative: Granular View of Customer Profitability by Sales Channel and, then Product Type



Case Study

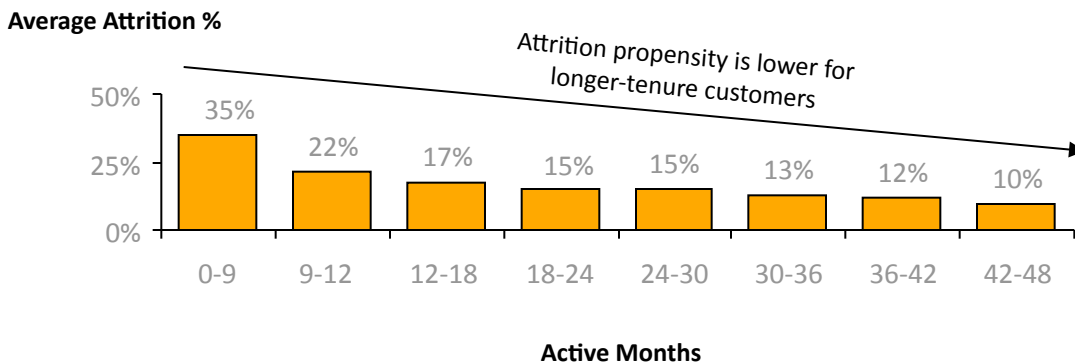
Growth-oriented companies often make the common mistake of overemphasizing customer acquisition, at the expense of investments in retaining existing customers – customers that potentially are much more profitable. One of our clients, a provider of telecommunications technology, had followed this customer acquisition path and had been actually quite successful in taking market share from competitors, albeit at increasingly lower prices and margins.

Perhaps unsurprisingly, the company discovered that the average revenue contribution of these newly acquired customers was significantly lower – by as much as one-third vs. older customers. Customers that had been retained for five years were four to five times more profitable than new customers.

How did the company unlock these insights? We helped them to examine five years worth of customer data – including acquisitions, retention rates and attrition – and analyzed the data by customer, pricing, acquisition date, and other elements. We looked at profitability metrics and then performed a correlation analysis to understand the factors that were driving retention and profitability.

Our analysis discovered that, contrary to the company’s assumptions, pricing was not the primary driver of attrition – longevity was. Attrition rates were high for new customers over the first six months, then fell slightly over the next six months, regardless of what price point these customers entered. From 9-12 months, the attrition rate was cut in half.

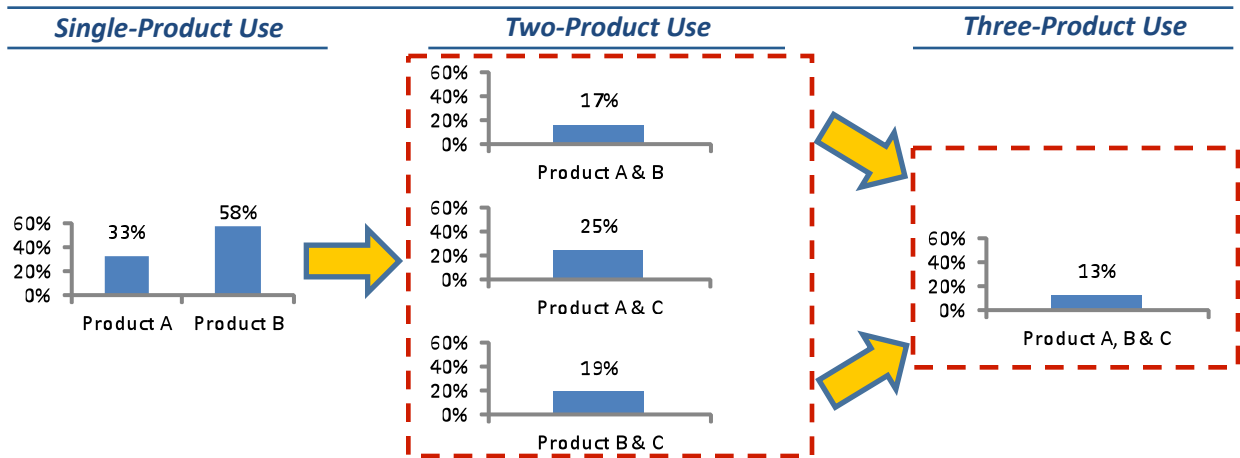
Attrition by Number of Active Months



Over the five-year span, new customers had a 50% chance of attriting in year 1, while those who remained had a 50% chance of attriting over the next four years. The attrition rate of customers who had been with the company four years or longer dropped to less than 10%.

The number of products a customer purchased also had an impact on attrition rates. If they bought two products, the attrition rate was cut in half. If they purchased three products, attrition was cut in half again.

Churn by Multi-Product Usage



The path was clear: The company needed to reallocate its marketing spend around retention and cross-sell programs for existing customers, and de-emphasize customer acquisition programs. The marketing and sales teams were realigned around programs to reduce attrition and attract and retain more profitable customers. The company invested more in customer service and began taking pre-emptive pricing actions with the customers it identified as the most profitable. It began investing more in cross-sell campaigns designed to sell a second or third product to existing customers – thus reducing their likelihood of attrition. And the company stopped reducing prices to the point of unprofitability.

In the end, we were able to provide a recommendation on key activities to create value through reducing attrition.

<i>Potential Attrition Reduction Opportunities</i>		<i>Estimated Value Impact</i>
A	Impact Attrition through product offering	\$40-60MM
B	Impact through Identifying near-term high-risk customers - Automate the “red flagging” and increase investment in turning around “red flagged” customers	\$40-60MM
C	Address key sources of customer dissatisfaction	\$10-15MM
D	Focus customer acquisition investment on lower-attrition segments	\$5-10MM
Potential “No Regrets” Value Impact from Addressing Attrition:		\$95-145MM

Summary

In this difficult economic environment, companies can struggle to identify profitable growth and margin improvement opportunities. The good news is that the opportunities are close at hand – with your existing customer base. Mining existing customer data can unlock a range of new growth opportunities. Measuring customer profitability and identifying the drivers of customer profitability will help you identify profitable growth and margin improvement opportunities to pursue in order to keep your most valuable customers coming back for more.

Formation of Avondale Strategic Partners

We are pleased to announce the formation of Avondale Strategic Partners (ASP). ASP was formed to actively partner with owners of middle-market businesses, through management-assisted buyouts, to create value through the generation of profitable incremental growth, supported by a sound strategic plan. It is our belief that collaboratively developing a robust strategic plan that clearly identifies opportunities for value creation and provides a clear path to capturing the value through detailed action plans is critical to the creation of equity value in middle market companies. Unlike a traditional private equity group or financial investor, we are able to leverage Avondale’s proven track record in helping companies develop a strong and achievable strategic plan to create shareholder value. We focus on building value through:

- i. aligning management and investors around a common value improvement goal;
- ii. developing a fact-based set of strategic priorities for value growth;
- iii. rigorously evaluating strategic alternatives around those priorities; and
- iv. applying a disciplined execution model to achieve incremental growth and profitability

Our professionals have created significant value at a wide range of leading Fortune 500 companies and have developed a unique skill set for assisting management teams in creating value. Through ASP, we are committed to leveraging these resources through a partnership with management to drive long-term value creation.

Our proactive and collaborative approach with management makes Avondale Strategic Partners an ideal partner for business owners and management teams seeking to drive significant equity growth. ASP’s hands-on approach benefits investors and business owners alike, as it dramatically increases the likelihood of a successful investment. By acquiring a majority (or significant minority) stake in the business, our incentives are clearly aligned with the business owner’s objectives.

Avondale Strategic Partners’ philosophy is to:

- Partner with management to develop and implement a corporate transformation aimed at achieving sustainable value growth, through the creation and implementation of a true strategic plan
- Provide management of middle-market businesses with the strategic, operational and financial resources necessary to effectively execute the corporate transformation
- Jointly with management, hold the organization and specific individuals accountable for the implementation of the strategic plan and for achieving specific targets for intrinsic value improvement
- Create an opportunity for key employees, the company’s most important assets, to participate in the ownership and success of the company

In order to maximize the impact of our partnership, we focus on investing in businesses with revenue between \$10 and \$100 million and EBITDA between \$2 and \$10 million and, most importantly, a management team that recognizes the benefits of a strong partnership with a team offering deep experience in assisting companies maximize value. Although we have an expertise in a number of industries, including niche manufacturing, specialty parts suppliers, injection molders, printers, food and beverage manufacturers and co-packers, and consumer product distributors, we are industry agnostic and will evaluate opportunities in new segments where we feel our skill set adds value.

For more information on Avondale Strategic Partners please visit www.avondalestrategicpartners.com or contact Rob Crisp via email at rob.crisp@avondalestrategicpartners.com or phone 312.371.6030

Avondale Connections

Rob Crisp Joins Avondale

Avondale is pleased to announce that Rob Crisp has joined as Managing Director of the newly formed Avondale Strategic Partners. Rob brings nearly fifteen years of investment banking and M&A advisory experience to the team and leads Avondale’s M&A advisory practice.

Rob was formerly the CEO and Co-Head of Mergers and Acquisitions at Crowe Capital Markets in Chicago. He earned his MBA from the Kellogg Graduate School of Management and his bachelor's degree from the University of Illinois.

About Avondale

Avondale advises corporations on how to create **profitable growth** and increase the financial value of their business. Avondale works with senior management teams across a range of industries to develop practical and actionable solutions that sustain long-term value creation.

Contact Avondale

For more information on Avondale, contact one of the Principals or visit www.avondaleconsulting.com.

Karl Stark	karl.stark@avondaleconsulting.com	• Phone: (312) 953-7372
Bill Stewart	bill.stewart@avondaleconsulting.com	• Phone: (858) 231-2353
Greg Stoklosa	gregory.stoklosa@avondaleconsulting.com	• Phone: (847) 778-7102
Rob Crisp	rob.crisp@avondaleconsulting.com	• Phone: (312) 371-6030