PRIVATE EQUITY PERFORMANCE IMPROVEMENT

Challenge 2025 for PE – The Rapid Growth Roadmap: Actions that Matter Now

"If you don't drive your business, you will be driven out of business" – B.C. Forbes

This article is Part 2 in a series on creating value in portfolio companies. Read Part 1 here.

How many of your portfolio companies are hanging on by life support as you patiently wait for market conditions to improve? Unfortunately, many of the present-day economic conditions — high interest rates, labor costs and supply chain destabilization — will largely continue while your profitability languishes or wastes away.

Reviving profitability by acting now requires a much more aggressive remediation of underperforming companies and a pivot back to value creation.

How? Below is a roadmap to a three-fold successful recovery: rapid growth, improved margins and unlocked trapped cash.

In this commercial-focused deep dive into Private Equity (PE) value creation, we present the Rapid Growth Roadmap: five questions investors, CEOs or Boards should ask to effectively identify and realize near-term growth opportunities.

PE funds who include these initiatives in their portfolio strategies can breathe new life into their growth initiatives, even as they wait for economic conditions to stabilize.

Ground Growth Plans in Fact-Based Data and Insights

In a recent article, "Challenge 2025 for PE – Action that Matter Now," our colleagues Markus Lahrkamp and Charles Lowry unequivocally stated that private equity (PE) funds must take decisive action. By working with portfolio companies to implement aggressive value creation strategies, they can enable struggling companies to survive and, later, thrive. These value creation programs are often all-encompassing, ensuring that the entire company works together toward aligned objectives.

Within the commercial organization, this edict translates to a specific focus on identifying and capitalizing on the most profitable market opportunities and pulling back on those that are profit dilutive. The trick to this, however, is knowing *how* to identify profitable opportunities and being able to plan to act quickly. Given this challenge, it is essential that leaders ground revenue plans in market insights and data, using an objective fact base to drive critical commercial decisions and gain clarity on how the commercial model will successfully meet expectations without relying on ungrounded optimistic performance outlooks. As the great football coach Vince Lombardi stated, "Hope is not a strategy. Fear is not an option."

Therefore, it is imperative that PEs and their portfolio companies focus on profitable growth from the core of the business. This means optimizing value from existing customer segments and product portfolios rather than seeking hard-to-execute and risky adjacencies, product line expansions, step-outs or blue-sky strategies.

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The Rapid Growth Roadmap's Five Central Questions

Each of the Rapid Growth Roadmap questions provides PE funds and their portfolio companies with new perspectives on and clarity into their customers, strategies and market position. This enables PE firms to quickly execute in-market strategies to drive the growth needed to enable struggling portfolio companies to change their trajectory, positioning them for success.

1. Do you know *which customer segments* are most attractive and how effectively your commercial organization is positioned to win within these segments?

Know your customers — Companies often simplistically segment their customers into large, medium and small groups, based solely on their history with these customers. This narrow view often leads to inadequately prioritizing investment across channels and roles. Instead, companies should utilize additional market data in customer segmentation to better understand an account's true profit potential and attractiveness. Segmenting customers the *right way* — based on the intersection of profit potential and right to win — enables the most productive lead generation and conversion approaches, unique value propositions and messaging. It also allows for the highest value-pricing potential while appropriately aligning cost-of-acquisition and cost-to-serve with upside. This segmentation and prioritization approach can reposition a company's market coverage model and focus to maximize return on investment without delay.

2. To what extent *does your portfolio strategy help drive decisions* on how you sell or serve tail offerings?

Smartly deploy your portfolio — The sales function is often focused, rightfully, on the largest product lines. However, this over emphasis can lead to an inadequate understanding of the performance and portfolio role of "tail SKUs," products and services that make up a smaller portion of sales. These tail items often drive additional operational complexity and higher cost-to-serve; however, they tend to fly under the radar and enjoy the same standard discounts and terms and conditions as the larger and more accretive product lines. To survive the present and reposition for growth, it is critical to tease out the margin performance of tail SKUs, assess their strategic necessity and drive higher volume and higher pricing. SKUs that can't improve top-line contribution or stem profit dilution should be rationalized.

3. Do you know *which customers are most susceptible to attrition and why,* so that you can intervene before it is too late?

Sound the alarm on churn — Sales representatives often track their own customers closely and have heightened awareness of churn risk based on various factors — such as quality, reliability or fulfillment satisfaction, competitor pricing actions and product introductions — even if these details may not be flashing red in customer relationship management (CRM). Additionally, it is much more likely for struggling companies to chase growth by over focusing their investments and actions on acquiring new customers and neglecting to predict the core drivers of churn and risks to reduce attrition. Since attrition often points to underlying issues, including poor pricing, inadequate customer support or competitive inroads that are observable and predictable, PE firms should formalize a customer retention program that:

- Tracks leading indicators such as spend, purchase frequency, customer support issues and invoiced prices;
- Analyzes trends and establishes and quantifies specific churn drivers;
- Sets up a cross-functional review of churn drivers and attrition risks; and
- Develops, tests and refines interventions to stem market attrition.

These well-founded retention programs are the key to lessening pressure on acquisitions and offsetting customer attrition.

4. Do you know *how to maximize share of wallet from existing customers* through cross-sell and up-sell across your offer portfolio?

Hone better selling initiatives — Struggling companies often choke on the breadth and complexity of their offer portfolios, though they tout them as a competitive advantage. While companies understand the cost and operational challenges of this diversity, they unsuccessfully maximize revenue promised by their portfolio offerings. This can be overcome through analytical rigor and behavioral change sponsored from the very top of the organization. Market basket analyses can quickly identify the cross-purchase likelihood between offers, enabling more effective bundling, as well as highly personalized offers to expand share of wallet. The theoretical potential of the analysis can be unlocked by commercial teams primed to take advantage of these insights. Therefore, it is essential to launch cross-sell and up-sell initiatives with quantified targets, incentives and program governance that encourage the desired behavioral changes, rewarding those who commit.

5. Is your approach to *pricing strategy, execution and governance maximizing prices* or leaving money on the table?

Reassess your pricing — While price setting based on incremental customer value is critical, organizations must first capture tactical price increases that can boost margins. There are often unexplainable discount variations between representatives and across customers as well as a lack of disciplined approval processes. Though companies do pass input cost increases to customers through pricing, they do not do it often or enough and tend to evenly spread them across customer groups when they do. As a result, companies leave money on the table in specific customer relationships. There is a considerable surgical pricing opportunity that can be easily captured with a solid business case, scripts for the sales teams and governance models that carefully track price increase communications and customer responses. These tactical actions can also serve as the foundation for broader value-based pricing initiatives that enable continued growth over time.

Bringing the Rapid Growth Roadmap to Life

In a recent buy-side study of a healthy specialty industrial distributor — with approximately $500 million, or 20 percent, EBITDA — the Rapid Growth Roadmap identified approximately $9 million in tactical EBITDA enhancement opportunities that could be realized through quick actions to drive customer retention, increase cross-sell and enable more disciplined pricing across the sales force. Given the near-term potential for growth, the acquirer successfully underwrote a sizeable portion of this value creation growth opportunity in its investment thesis.

How Can A&M Help?

Across client contexts, A&M has used the five central questions of the Rapid Growth Roadmap to enable decisive commercial actions that drive growth and EBITDA in the short- to medium- term for struggling portfolio companies. While upside realization varies from situation to situation, we often collaborate with clients who achieve between 500 bps to 800 bps of margin improvement by activating these close-in levers. Additionally, the Rapid Growth Roadmap often serves to fund future growth endeavors related to new markets, new customers, new offers and more sophisticated and time-intensive commercial effectiveness endeavors, such as pricing to value and broader sales force transformation.

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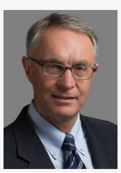

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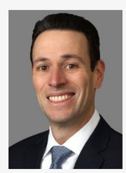

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