LEK

Know Thy Subscriber:

Putting Your Data to Work on Retention and Monetization

1. Leverage your data to maximum advantage
2. Boost long-term success
3. Gain foresight on customer behavior
4. Build intervention events to change outcomes
5. Overcome data silos for greater insight

Optimize customer costs

As any subscription-based business knows, customer churn can be a major drag on growth. Not only are customers expensive to replace — a common rule of thumb is that acquiring a new customer costs five times as much as keeping an existing one — but new customers can also be harder to cross-sell/up-sell to.

That's why growth-minded businesses place extra emphasis on customer retention and existing account monetization. While many organizations have a good grasp on how they perform on retention or cross-sell/up-sell, a key challenge is knowing when a customer is likely to take either kind of action so you can respond accordingly.

Real-time, predictive analytics can be the answer to minimizing attrition, maximizing cross-sell/up-sell and ultimately driving significantly improved revenue metrics.

How churn and cross-sell/up-sell affect net revenue retention

Net revenue retention (NRR) is one of the most critical metrics for any subscription business. NRR is calculated by adding your starting monthly recurring revenue (MRR) to the change in MRR (expansion less contraction and churn), and then dividing by the starting amount.
The formula is expressed as:

$$\frac{\text{starting MRR} + \text{expansion} - \text{contraction} - \text{churn}}{\text{starting MRR}}$$

It costs 5 times as much to acquire a new customer as it does to retain one

Companies can significantly boost their long-term success and corporate valuation by improving their NRR

How significantly? According to our analysis, NRR explains almost half of a company's variance in enterprise value to revenue multiples. Each percentage point increase in NRR is associated with a 0.5x change in multiple.

Net Revenue Retention = Long-term success

NRR

Relationship between NRR and EV/revenue multiple for public SaaS companies (April 2022)

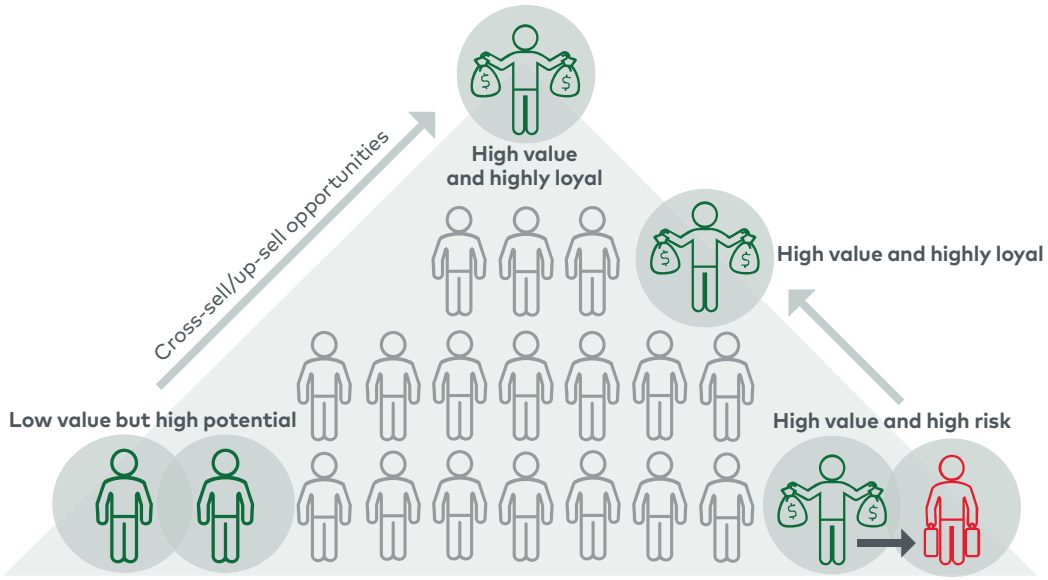
*Net revenue retention = (Revenue at the start of period + upsell – downsell – churn) / Revenue at the start of period
Note: Includes all public SaaS companies in BVP's Emerging Cloud Index that have NRR data available; R-squared for line-of-best-fit=0.40; regression coefficient on NRR=0.53; NRR=net revenue retention; EV=enterprise value; SaaS=software as a service; LTM=last twelve months
Source: BVP; public company listings; L.E.K. Consulting research and analysis

Gain foresight on customer behavior

Most organizations have some way to track customer churn numbers at an aggregate level, and some may run analytics to explain why the churn happened. But this information is hindsight — it only gets you so far toward truly moving the needle on NRR. It takes foresight to understand when churn may occur so the business can mitigate the problem before it happens. A similar situation exists with up-selling and cross-selling, where opportunities are often overlooked until they're lost.

L.E.K.'s predictive, machine learning-driven models provide foresight on customer behavior so you can see how specific accounts are likely to perform (e.g., is Customer X at risk? Is Customer Y ready for an upgrade?).

Predictive analytics that minimize churn and increase customer revenue



Segmentation of customers based upon "propensity" scoring
(e.g., 100s to 10,000s of customers)

Source: L.E.K. research and analysis

Flagging sales opportunities and attrition risk for an information services provider

A leading information services provider asked L.E.K. Consulting to build a machine learning-driven model to predict when customers were likely to either leave the company or make a new purchase so the company could take appropriate action.

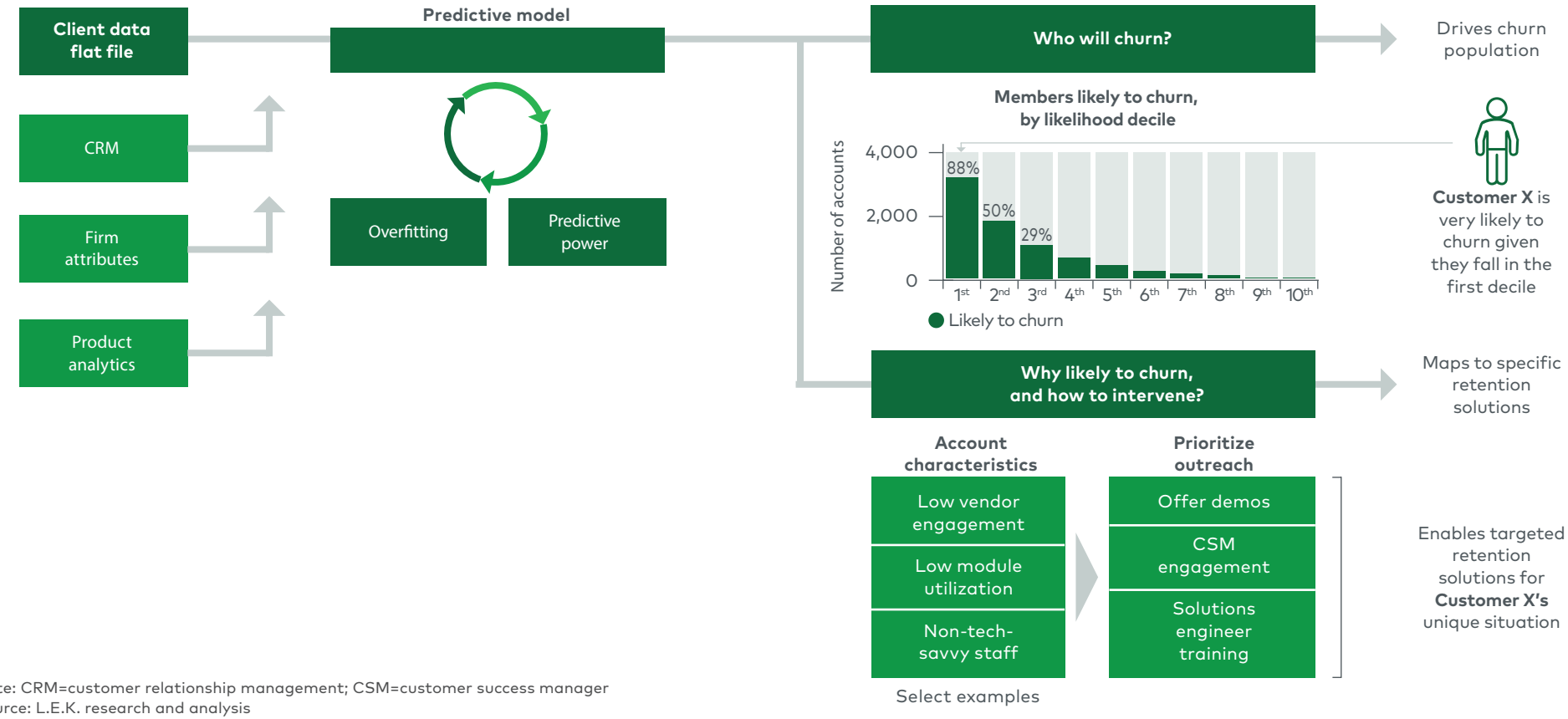
We built a propensity model to score customers on their monetization potential and attrition risk. This involved developing 12 different machine learning models and testing them on a master data set of the company's customer accounts. From there, we collaborated with our client to select the best-performing model.

Now our client runs this predictive model daily. Dashboards show the customer accounts flagged for intervention. Meanwhile, sales managers get alerts about accounts whose status has changed, with tailor-made intervention steps to drive changes in behavior.

Mitigation steps are embedded into your Customer Success team's workflow

Furthermore, knowing what customers are likely to do is only half the story. Knowing which intervention events will actually change an outcome is equally critical. By analyzing historical data and working with your Customer Success team, we define and embed mitigation steps into your employees' workflow. These steps propose tailored interventions for each account, and they are becoming increasingly smart over time as more data is generated and analyzed.

Example model design and overview of the L.E.K. engine



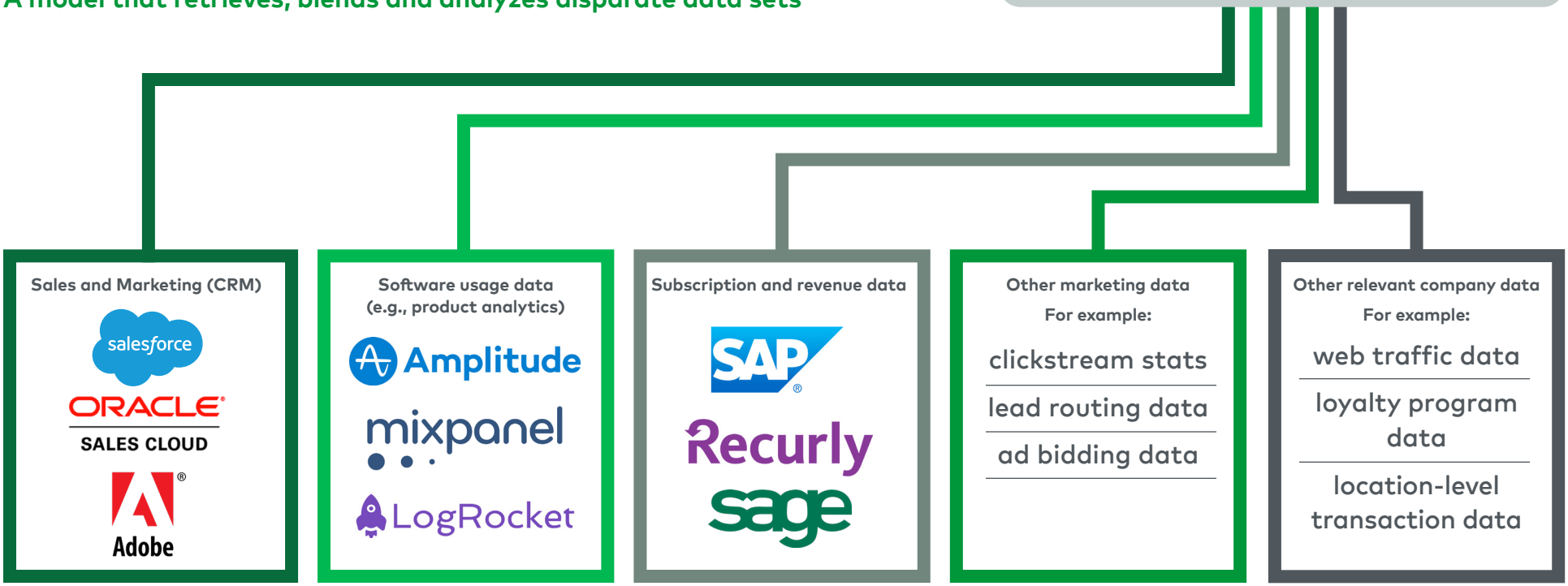
Note: CRM=customer relationship management; CSM=customer success manager
Source: L.E.K. research and analysis

Overcome data silos for greater insight

A subscription business has a treasure trove of customer data. But internal silos can prevent the organization from using all the relevant data at its disposal. Our model seamlessly combines data from multiple platforms as well as high-value external data sets to create a single view for analysis.

Our model seamlessly combines data from multiple platforms to create a single view for analysis.

A model that retrieves, blends and analyzes disparate data sets



Note: CRM=customer relationship management
Source: L.E.K. research and analysis

Harmonizing data sets maximizes the model's predictive power and unlocks cross-functional insights (think product usage and how it affects optimal cross-sell/up-sell strategy). It also improves the model over time by continuously adding new data to mitigate problems and capture opportunities.

Improve your customer retention and profitability

As important as it is to acquire new customers, it's ultimately more effective and efficient to monetize the customers you already have. And that makes customer retention an equally important priority.

With L.E.K.'s predictive modeling capabilities, you can gain both insight and foresight on how to optimize your company's NRR for long-term success.

For more information, please contact:
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About L.E.K. Consulting
We're L.E.K. Consulting, a global strategy consultancy working with business leaders to seize competitive advantage and amplify growth. Our insights are catalysts that reshape the trajectory of our clients' businesses, uncovering opportunities and empowering them to master their moments of truth. Since 1983, our worldwide practice — spanning the Americas, Asia-Pacific and Europe — has guided leaders across all industries from global corporations to emerging entrepreneurial businesses and private equity investors. Looking for more? Visit **www.lek.com**.

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